States of Jersey

DRAFT BUDGET STATEMENT 2014

Embargoed until after delivery of the Treasury and Resources Minister's Statement on Tuesday 8 October 2013

TREASURY & RESOURCES

States of Jersey

DRAFT BUDGET STATEMENT 2014

Proposition

Draft Budget Statement 2014

The States are asked to decide whether they are of opinion:

(a) to approve, in accordance with the provisions of Article 10(3)(a) of the Public Finances (Jersey) Law 2005, the estimate of income from taxation during 2014 of £639,513,000 as set out in Summary Table A of the Budget Statement, with the sum to be raised through existing taxation measures and the proposed changes to income tax, Goods and Services Tax, Impôts duty, Stamp Duty and Land Transaction Tax for 2014 as set out in the Budget Statement.

(b) to approve, in accordance with the provisions of Articles 10(3)(c) and 11(3) of the Public Finances (Jersey) Law 2005 the appropriation of £2,210,000 in 2014 and £1,460,000 in 2015 from the amount appropriated to growth expenditure in the Medium Term Financial Plan 2013 to 2015 to a revenue head of expenditure for each States funded body as set in the recommended allocation of growth expenditure in Summary Table B.

(c) to approve, in accordance with the provisions of Article 10(3)(d) of the Public Finances (Jersey) Law 2005, a capital head of expenditure for each of the capital projects for States funded bodies to be started or continued in 2014 (other than States trading operations) as set out in the recommended programme of capital projects in Summary Table D totalling £88,892,000.

(d) to approve, in accordance with the provisions of Article 10(3)(e) of the Public Finances (Jersey) Law 2005, each of the capital projects that are scheduled to start during 2014 in the recommended programme of capital for each States trading operation, as set out in Summary Table E that require funds to be drawn from the trading funds in 2014.

(e) to agree –

(i) that, following the approval by the States on 16th May 2013 of the proposition "The Reform of Social Housing" (P.33/2013) and in accordance with the provisions of Articles 10(3)(b) and 21 of the Public Finances (Jersey) Law 2005, the States be authorised to borrow up to a maximum £250 million in 2014 for housing purposes and that, in accordance with the provisions of Article 10(3)(f) of the Public Finances (Jersey) Law 2005, the amount borrowed by the States be transferred from the consolidated fund to the Housing Development Fund;

(ii) in accordance with Article 3(3)(b) of the Public Finances (Jersey) Law 2005 that the purposes of the Housing Development Fund ("the Fund") be varied to enable the further provision and development of housing in Jersey and that –

(A) the Fund be permitted to lend money up to a maximum £250 million to Housing Trusts/Associations/Companies or bodies with the same purpose registered in Jersey in order that they can provide housing for islanders, on terms and conditions to be agreed, after consultation with the Minister for Housing, between the Minister for Treasury and Resources, and the aforementioned Housing Trusts/ Associations/Companies;

(B) all administrative costs associated with the operation and maintenance of the activities of the Fund to be paid out of the Fund;

(C) the fund to be invested through the Common Investment Fund in accordance with its own published investment strategy.

and that subject to the sanction by Her Most Excellent Majesty in Council and the subsequent coming into force of new Articles 3(3)(aa) and 3(3)(ab) of the Public Finances (Amendment No. 4) (Jersey) Law 201-

(D) all money due to the Fund, including any loan repayments and interest due from Housing Trusts/Associations/Companies, be credited to the Fund;

(E) money credited to the Fund does not form part of the annual income of the States.

(f) to refer to their Act dated 5th December 2006 in which they approved a revised policy for the use of the Strategic Reserve Fund established under Article 4(1) of the Public Finances (Jersey) Law 2005 and agreed that the Fund should be a permanent reserve, where the capital value was only to be used in exceptional circumstances to insulate the Island's economy from severe structural decline such as the sudden collapse of a major Island industry or from major natural disaster and to their Act dated 6th November 2009 in which they varied that policy and agreed that the Fund could be used if necessary, for the purposes of providing funding, up to a maximum £100 million to meet the States contribution to the Bank Depositors Compensation Scheme and/or to meet any temporary cash flow funding requirements of the Scheme established under the Banking Business (Depositors Compensation) (Jersey) Regulations 2010 and, in order to enable the creation of new hospital services as part of the proposals agreed by the States on 23rd October 2012 in adopting the proposition "Health and Social Services: a new way forward" (P.82/2012) –

to agree, as an exception to the approved policy for the use of the Fund, that the Fund may be used for the planning and creation of new hospital services in the Island, and to approve the transfer of an initial sum of £10.2 million from the Strategic Reserve Fund to the consolidated fund in 2014 so as to provide for these purposes, in accordance with the provisions of Article 4(3) and 10(3)(f) of the Public Finances (Jersey) Law 2005.

Minister for Treasury and Resources

Contents

Index of Figures

PART A – INTRODUCTION

1. 2014 Budget Foreword From The Minister For Treasury and Resources

Introduction

The measures proposed in this draft Budget for 2014 form a package that is designed to support the aims of economic growth and job creation.

This is a Budget that cuts taxes and invests in essential infrastructure for the long-term benefit of the Island.

It is a Budget that gives something back to the hardworking people of Jersey, who have carried on through difficult economic times.

It is a Budget that supports the Island's aspirations for economic growth, job creation, better education, better healthcare, and the development of infrastructure for the long term benefit of Islanders.

Worldwide Economic Recovery

There have been some positive economic developments at the global level in recent months. The Organisation for Economic Cooperation and Development (OECD) has stated that,

> *"the pace of recovery in the major advanced economies improved in the second quarter"*

and that,

> *"activity is expanding at encouraging rates in North America, Japan and the United Kingdom, while the euro area as a whole is no longer in recession."*

However, they also note that growth has slowed in several emerging economies and conclude that while recent improvements are welcome,

> *"a sustainable recovery is not yet firmly established and important risks remain"*

Overall, the OECD expects that the improvements in growth seen in the first half of 2013 will be maintained for the rest of the year.

They also emphasise though, that there is still risk, while the Euro area remains vulnerable to renewed financial, banking and sovereign debt tensions, and the potential remains for withdrawal of quantitative easing in the US.

The OECD policy advice at the global level is to continue to support demand in order to reduce the risk that the recovery will be derailed.

In the UK, the Bank of England has stated that a recovery appears to be taking place but that it will remain weak given the continuing post financial crisis process of adjustment and repair.

With this in mind the Monetary Policy Committee has adopted a new approach to monetary policy, providing explicit guidance regarding the future conduct of monetary policy. That is, that it intends,

> *"at a minimum to maintain the present highly stimulative stance of monetary policy until economic slack has been substantially reduced, provided this does not entail material risks to price stability or financial stability".*

A key consideration will be the unemployment rate and whether it has fallen below 7%.

Jersey Can Now Take Advantage of Its Strong Balance Sheet

In 2012, economic activity in Jersey fell by 4 per cent in real terms, representing the fifth consecutive annual fall.

The overall fall was a result of declines of -5% for the financial services sector and -4% for the non-finance sectors. Although GVA per capita fell in Jersey in 2012 to £36,700 it was still about two-thirds greater than that in the UK of £21,900. The latest survey information for the second quarter of 2013 shows that business activity is improving in the finance sector.

While the news remains negative for the non-finance sector, it is the least negative since September 2010. The headline business activity indicator has improved since September 2011. Five of the ten indicators for the finance sector improved and 7 of the 10 indicators for the non-finance sector improved in the second quarter.

Recent labour market data for Jersey has also been more positive. In particular, real earnings have increased for the first time in four years. Average earnings growth in June 2013 was 2.2%, 0.7% higher than in June 2012 and also 0.7% higher than inflation. This is an early indication that economic trends in 2013 have improved significantly relative to those in 2012 when average earnings growth was 1.5% less than RPI.

However, unemployment reached a new high level early in 2013 and has since remained stubbornly high.

Whilst 2012 saw total employment fall slightly from the record highs of 2011, the overall figure masks an increase in part-time employment at the expense of full-time employment.

Fiscal Policy Panel

The Fiscal Policy Panel (FPP), in their 2012 annual report (published in October 2012), forecast further declines in GVA in both 2012 and 2013 – of between 1 per cent and 3 per cent – with risks remaining to the downside. The FPP will be publishing a new Report (planned for 5th November 2013) in which they will comment upon the proposals within this report , Budget 2014.

This represented a downgrade from their previous forecast, on the basis of the continued deterioration in the economic situation within the Island and externally, and sluggish demand as a result of fiscal constraints in many of the advanced economies.

The FPP provide important independent advice for the planning of our finances.

Last year, in the context of a slightly downgraded economic outlook for Jersey in 2012 and 2013, the FPP highlighted seven key recommendations, all of which have been considered as part of this budget.

This Budget is framed against the international backdrop, local economic developments and the advice of the FPP. It supports our key economic objectives of:

- Supporting the economy in the short-term;
- Creating new employment opportunities;
- Laying the foundations for economic growth; and
- Committing to essential investment in our infrastructure.

Progress Made in Tax Policy and Administration

This Budget also continues the work of modernising our tax system and administration, and introduces measures that will support a sustainable return to growth.

The Taxes Transformation programme is proceeding well. The Taxes Office introduced online submission of personal tax returns (for taxpayers using agents) from January and online payments from February this year, while other projects involving internal data processing and ITIS (Income Tax Instalment System) improvement were also started and completed in 2013.

Other projects have also been started, and will have reports completed before the end of 2013. They include:

- Data and information exchange;
- Risk-based approach to compliance; and
- Organisational restructuring.

In addition, substantial work has been carried out to make changes to computer systems ready for the implementation of Long Term Care.

On tax policy, work has this year focused on international matters such as the implementation of FATCA, reviewing independent taxation and modernising the tax law relating to pensions.

Tax Policy and Administration in 2014 and beyond

The main focus on work for the Treasury in 2014 will be the development of a long-term tax programme, which will be published alongside the 2015 Budget. This programme will define the way forward for Jersey's tax regime and will include a proposal to modernise and simplify the personal tax regime, including the introduction of independent taxation and consideration of self-assessment and current year basis of tax. It will be wider than personal tax and will include a detailed programme, for example, of the ongoing property tax review.

Protection of tax revenues will also be an important focus in 2014 through ensuring proper compliance with the new distribution rules.

Further work will also take place to support the Social Security Department in the collection of the Long Term Care contributions, from the 1st of January 2015, subject to the outcomes of the States' debate on this matter.

In addition to Long Term Care work, the Taxes Office plans to make online filing of personal tax returns available to all taxpayers during 2014.

Reports Published and Consultations Launched

Published alongside this draft Budget are two reports and a consultation all of which support this drive towards modernisation and encouraging economic growth.

1. The results of a review of the Tax Regime for High Net Worth Individuals.

2. A feasibility report into the introduction of Independent Taxation in Jersey.

3. The launch of a consultation regarding proposed changes to the tax law in relation to Pension Schemes.

High Net Worth Individuals

This year, the Tax Policy Unit was asked to produce an update report following the introduction in 2011 of the new tax regime for High Net Worth Individuals ("HNWI") to review the success of the new regime and recommend, as appropriate, any further changes.

The report concludes that the regime is working well and proposes that the current system remains in place without any major changes but will continue to be monitored to ensure that it continues to deliver its objectives.

In addition, the report has highlighted some refinements that can be made to enhance economic growth.

It is proposed that the Income Tax Law will be amended in the 2014 Budget to allow certain pre-2011 HNWIs to transition to the 2011 tax regime, provided they meet certain criteria, for example, the capacity to enhance inward investment and create jobs. This will potentially encourage HNWIs to relocate their investment portfolios and active businesses to the Island, generating tax revenues, fees and economic growth through spend and employment.

In addition, to ensure that the contributions maintain their value in real terms, the minimum contribution will be reviewed every three years with a view to increasing the HNWI's tax contributions in line with inflation.

The positive conclusion from this review is that the tax policy introduced in 2011 is working largely as intended and is benefiting Jersey's economy. Meanwhile, the measures introduced in this year's Budget take another step towards creating economic growth by encouraging more inward investment that would otherwise go to, or move to other jurisdictions.

Independent Taxation

As part of the tax system modernisation programme, the Tax Policy Unit was asked to review how Independent Taxation could be introduced into the Jersey system.

The term 'Independent Taxation' refers to the policy of taxing individuals as individuals, regardless of their marital status. In Jersey, there is currently a 'default' for married couples to be taxed jointly. There are also certain allowances that apply to married couples that do not apply elsewhere within the tax regime, resulting in different treatment between married and cohabiting couples.

While married people have been able to opt for separate assessment, rather than joint, since 2003, it is recognized that the tax regime should adapt and evolve so that each individual is treated equally for tax purposes.

It is a widely accepted principle that our tax system should be both efficient and equitable, and that tax policy should not be used to encourage or discourage lifestyle choices; individuals or couples, whether married or cohabiting, should be treated equally. Independent taxation is therefore an important aspect of tax modernisation and provides for the needs of today's families.

This principle of a move to Independent Taxation makes sense in a modern society. However, it is vital that the logistical, administrative and financial impact of this change is managed correctly and makes the tax system simpler.

We are now committed to moving towards Independent Taxation.

However, it is vital that the logistical, administrative and financial impact of this change is managed correctly and makes the tax system simpler. It cannot be achieved, equitably, overnight - it needs a phased approach.

It is proposed that a first important step towards Independent Taxation will be made in this year's Budget by bringing the Marginal Tax Rate and '20 means 20' into closer alignment. This is covered in more detail under 'Specific Budget Measures for 2014'.

Work will now continue on designing an ambitious plan to introduce Independent Taxation to the following timetable:

- Review completed and recommendations included in the 2016 Budget at the end of 2015.
- Commencement of implementation in 2016.
- Implementation fully completed by 2020.

This timetable is based on the assumption that the cost of introducing Independent Taxation, be that to taxpayer or the States, will be acceptable to the States.

In addition, a detailed long-term tax programme will be published in 2014 alongside the 2015 Budget, which will include the Independent Taxation review as well as matters such as self-assessment and current year basis. Consideration will be given to including further changes in the 2015 Budget to facilitate the move towards Independent Taxation.

Tax Policy and Pension Schemes

A consultation is being launched alongside the Budget regarding proposed changes to the tax rules applying to pensions and pension schemes.

Because the interaction of taxation and pensions is inherently complicated, the proposed amendment to the Income Tax Law is being published as a consultation draft. It is hoped that a wide range of interested parties will take the opportunity to review the proposed changes before they are lodged with the States, facilitating the enactment of the most appropriate set of tax rules.

In addition to the proposed amendment, the consultation seeks views on a small number of additional pension related topics. Following completion of the consultation, the comments received in relation to these topics will be analysed and any amendments considered appropriate will be included in next year's Budget.

Specific Budget Measures for 2014

The Medium Term Financial Plan agreed by the States assumed that no significant tax policy changes would take place for a further two years and the proposals in this proposed Budget are consistent with that. This Budget continues to provide the stability and certainty needed, and builds on those foundations to enable growth.

The focus of the 2014 Budget recommendations is to stimulate economic growth by:

- Maintaining the cornerstones of the existing tax regime to promote stability for business.
- Putting more money in the pockets of taxpayers through a reduction in the marginal rate and increases in exemption thresholds.
- Encouraging further inward investment through changes to the tax regime for High Net Worth Individuals.
- Provide targeted tax breaks for parents of children in higher education so as to develop a skilled future workforce.

In addition, there is a strong focus on ensuring the tax law works as intended.

Income Tax

Explaining Marginal Relief

Personal income tax in Jersey is based around a standard 20% rate of tax with limited deductions and allowances.

However, to protect the lower to middle income earners, a separate calculation called ‘marginal relief’ is also performed using the exemption thresholds.

Further deductions like mortgage interest relief and child care relief may also be taken into account in the marginal calculation.

Taxpayers whose total income is in excess of their exemption threshold fall into what is termed the ‘marginal band’.

The calculation of their liability to tax at the marginal rate of 27% ensures that there is no disproportionate increase in their tax bill if their income exceeds their exemption threshold.

Because of these exemption thresholds being used in the calculation of tax (increased as appropriate by the above allowances or reliefs) it is only those with high incomes who do not benefit from them.

This means that if in any year someone’s total income is less than the exemption threshold, the percentage of tax you will pay on that income will be 0%.

As someone’s income increases or their circumstances change, the percentage of tax you pay will increase as the marginal relief gradually tapers away until you are paying the maximum 20%.

The practice in recent years has been to increase the exemption thresholds by reference to the lower of the RPI figure and the annual increase in earnings.

Although in both the 2012 and 2013 Budgets, thresholds were increased by slightly higher amounts.

Tax Cuts – Giving Back

Our strategic approach to fiscal policy, in response to both the changes in our corporate tax regime and the need to repair revenues after the global financial crisis, has been consistent:

- Focused on raising revenue through indirect taxation; and
- Recognising the risks that other forms of taxation pose to the economy.

Having taken these difficult decisions in the past and keeping our finances on a strong and sustainable footing we can now afford to give something back.

To achieve this we are proposing three bold measures, namely:

- Increase the income tax exemption thresholds;
- A reduction in the marginal rate of tax; and
- Increase the tax relief for parents in the marginal band with children in higher education.

Exemptions and Thresholds

The income tax exemption thresholds are income levels below which taxpayers do not have a liability to income tax. The practice in recent years has been to increase the exemption thresholds by reference to the lower of the RPI figure and the annual increase in earnings, although in both the 2012 and 2013 Budgets, thresholds were increased by slightly higher amounts.

For the 2014 Budget, it is proposed that thresholds are increased by 1.5%.

This will provide a direct financial benefit for approximately 84% of Jersey tax payers at a cost of approximately £2.5m.

Decrease in the Income Tax Marginal Rate

Additionally, this draft Budget proposes that the marginal rate of tax be cut from 27% to 26%.

Based on the 2011 year of assessment, this proposal will reduce the tax liability of approximately 84% of taxpayers (around 40,000 households) at a cost of approximately £7.8m.

The overall cost of a 1.5% increase in exemption thresholds, combined with a 1% decrease in the marginal rate, will be approximately £10.3m.

Enhanced Income Tax Exemption Threshold for Parents of Children in Higher Education

Additional support is proposed through an increase in the tax relief available to parents currently in the marginal relief bracket with children over the age of 17 years and in full-time higher education from £6,000 to £9,000 per child.

This will mean parents will benefit by up to £780 per child at a cost to the States of approximately £900,000.

In addition, the restriction to child allowance by reference to the child's earned income will be removed at a cost of approximately £420,000.

Changes to the higher exemption threshold

As announced last year, this year's budget proposes to increase the age of entitlement for single, married persons and civil partners to the higher exemption threshold from 63 to 65.

Income Tax Allowances for Standard Rate Taxpayers

It is proposed that income tax allowances for higher earners who pay tax at the standard rate are unchanged for 2014.

Changes to the tax regime for certain High Net Worth individuals

The change to the tax regime in 2011 for High Net Worth Individuals who are granted housing licences under regulation 1(1)(k), now 2(1)(e), was designed to encourage more inward investment to the Island. This budget proposes to take this further by allowing existing residents with housing licences granted under regulation 1(1)(k) to apply to be taxed under the new rules introduced in July 2011 on a discretionary basis, in order to create new employment and investment opportunities that could be created in Jersey by the transfer of business and investments from offshore to onshore, thereby encouraging economic growth.

Protecting revenues

There are a number of measures aimed at protecting revenues including strengthening the Comptroller's powers to effectively challenge tax relief claims for non-commercial debt structures.

Income tax administrative Changes

There are a number of proposed administrative amendments to the tax law to ensure that the law works as intended. This includes amending the ITIS provisions to restrict credit to controlling directors to eliminate potential unintended benefits, amending the rules relating to oil importation and distribution companies and revoking the three year rule of residence for qualifying Lump Sum Donations, among others.

Goods and Services Tax

There is no change in the rate of GST, which remains at 5%. Some minor administrative changes are proposed to ensure that the law works as intended. These measures include clarifying the definition of an 'Existing Building' that is eligible for the 0% rate, clarifying the position regarding white goods, carpets and other removable goods supplied in zero-rate dwellings, and providing increased flexibility in the deregistration process, among others.

Impôts Duty

The proposals for 2014 impôts duties take into account the economic conditions, inflation and the Island's tobacco and alcohol strategies, following consultation with the Council of Ministers and, in particular, the Ministers and Officers from Health and Social Services, Home Affairs and Economic Development.

The Budget proposals are set out in detail in the following document and will raise additional revenue of approximately:

Alcohol duties	£1,254,000
Tobacco duties	£1,466,000
Fuel duties	£399,000
Vehicle emission duty	£44,000

In summary, the proposed increases in the 2014 Budget are:

- Increase the duty on alcohol with:
  - 11% increase in duty on a litre of spirits – £1.27 per litre.
  - 5% increase in duty on a bottle of table wine – 7p per bottle.
  - 5% increase in duty on a pint of weaker beer and cider (not exceeding 4.9% abv) – 2p per pint.
  - 11% increase in duty on a pint of strong beer and cider (exceeding 4.9 abv) – 6p per pint.

- Increase on the duty on 20 king size cigarettes by 11% – 47p per packet of 20 cigarettes
- Increase on the duty on all fuels by 2% – 1p per litre
- Increase on all VED (Vehicle Emission Duty) bands by 5%

These measures support the Health Minister's drive to reduce the adverse effects on health of excessive alcohol consumption and smoking. It is proposed that the increases in duty will take effect from midnight on 31st December 2013.

Stamp Duty and Land Transaction Tax

The proposal in the 2014 Budget is to continue the extension of the maximum threshold for first-time-buyer relief from £400,000 to £450,000 until 31 December 2014.

Growth Proposals for 2014

In the debate of the Medium Term Financial Plan (MTFP P69/2012) in November 2012, the States agreed an amendment by the Chief Minister to the proposals by the Corporate Services Scrutiny Panel for a central growth allocation in 2014 and 2015.

The amendment by the Chief Minister resulted from a review by Ministers of those growth bids, which could be held centrally and allocated in future years' annual Budget.

The Council of Ministers is now proposing that the Allocation of Central Growth for 2014 of £2,210,000, and associated funding of £1,460,000 for 2015, be allocated to departments in line with the original allocation.

Capital Programme

The Medium Term Financial Plan (MTFP) set out the capital programme for each of the years 2013-2015 and the debate on the MTFP approved the capital programme, in total, for each of these years. The budget for each of these years will approve the detailed list of projects.

The total allocation approved for 2014 was £88,892,000.

The review of the proposed programme has identified a reduced cost for additional primary school accommodation. It is proposed that this variance is reallocated to accommodate an additional allocation to Transport and Technical Services for works at Green Street Car Park, Education Sports and Culture for work required to meet their Sports Strategy and Fiscal Stimulus and Parish Projects.

More detail of individual projects can be found in the main body of this document, but, departmentally, the approximate allocations for 2014 are:

Chief Minister's Department	£1.04m
Education Sport and Culture	£15.76m
Department of the Environment	£0.65m
Heath and Social Services	£14.73m
Home Affairs	£1m
Transport and Technical Services	£25.8m
Treasury and Resources	£2.5m
Other Capital	£5.2m
Social Housing Programme	£22.2m

Major Capital Projects: Hospital, Housing and Liquid Waste

The Island faces a need for major infrastructure investment in housing, hospital facilities and liquid waste infrastructure. This Report brings forward innovative and cost effective ways of funding these projects that will minimise the cost, maximise the use of existing resources and safeguard our Island for the long term.

A Budget to Support Growth and Create Jobs

At a time when unemployment remains at high levels, it is vital that the public sector does what it can to support the economy, particularly when private sector activity may take time to recover.

The 2014 Budget goes further than providing stimulus in the short-term and continues to provide support for the key policy areas of Back to Work and the Economic Growth and Diversification Strategy.

Back to Work will help to minimise the costs to both the individual and society of the current levels of unemployment and ensure we do everything we can to get those out of work, particularly the young back into employment as quickly as possible.

We must build for the future and lay the foundations for economic growth now, which will benefit us in the future.

This Budget provides support for the Economic Growth and Diversification Strategy in all key areas including:

- The new £5m Innovation Fund;
- Supporting the continued growth and diversification of the financial services sector; and
- New enterprise strategy that will deliver new high value and high growth business and raise the productivity of the whole economy.

The Minister for Social Security has already published a report in August on the new Long-term Care scheme that will help Islanders pay for care, either in their own home or in a care home.

If the States agree, the new long-term care scheme will start in July 2014, offering greater protection for hard working Jersey families.

However, although the benefits from the scheme would be available from next year, contributions to the scheme would not begin until 2015 at 0.5% of taxable income, rising to 1% in 2016.

To prevent money being taken out of the economy while it is still under pressure, the Treasury has worked with Social Security to make it possible to reallocate existing Social Security budgets so as to avoid the need to introduce a 1% contribution in 2014. Current proposals are to reduce the planned contribution to 0.5% in January 2015 and 1% from January 2016.

This will prevent a further squeeze on Islanders disposable incomes and at a time when we are supporting the economy through fiscal stimulus.

Additional Income Tax proposals

- Remove restrictions to child allowance by reference to the child's earned income.
- Increase the age of entitlement to the higher exemption threshold from 63 to 65.
- Amend ITIS provisions to restrict credit available to controlling directors.
- Create a level playing field for oil importation and distribution companies.
- Introduce mandatory online filing for ITIS returns.
- Remove 3 year rule of residence for making lump sum donations .
- Permit certain residents with housing licences granted under regulation 1(1)(k) to apply to be taxed under the post July 2011 regime.
- Strengthen legislation on interest deductions to counter non-commercial debt financing.

- Revise the relief due to the self employed in respect of social security contributions in response to changes to the social security law.

- Repeal the tax credit due for the electronic delivery of income tax returns.

- Amend the distribution rules introduced in the 2013 Budget to ensure they operate as intended

Conclusion

This is a Budget that cuts taxes and invests in the long-term infrastructure of the island. It balances the needs for short-term fiscal support to boost employment with the need to underpin economic growth and job creation policies in the medium term.

It provides the fiscal stability and certainty that will help growth flourish and at the same time commits to the essential investment the Island needs in areas such as health and housing.

Supporting the economy and investing to improve our competitiveness now will mean we are in the strongest position possible as the global economy continues to improve.

This is a Budget that provides direct financial relief to the majority of hardworking, taxpaying islanders, and helps to get money back into the economy.

This is a Budget that reflects the emerging signs of economic growth around the world, and positions Jersey to take advantage of these improvements.

I commend this Report, Budget 2014 and associated papers in Independent Taxation, High Net Worth Individuals and Pensions to the States Assembly.

Philip Ozouf

Senator Philip Ozouf
Minister for Treasury and Resources

October 2013

PART B – BUDGET STATEMENT 2014

2. Income Tax Proposals

Background

The Minister for Treasury and Resources considers annual Budget measures so as to ensure the States revenues are sufficient to meet spending proposals. The spending proposals were set out for three years from 2013 to 2015 in the MTFP adopted last year.

The tax proposals in the 2014 Budget seek to support the key Strategic Plan themes of creating employment and economic growth.

The economic climate remains challenging for both individuals and businesses. The proposals in this Budget seek to maintain certainty and stability in the tax regime for Business so that businesses can focus on growth, which can lead to increased employment. It goes further in providing additional help to individuals through the reduction in the marginal rate of tax which is also an important first step towards modernising and simplifying the personal tax regime.

The commitment not to increase income taxes and GST during the period of the MTFP is being maintained. There are no changes in this Budget to the cornerstones of Jersey's tax regime, being the general rate of 0% for companies, a standard rate of income tax of 20% and 5% GST.

It is important to ensure that the tax system operates as intended. Many of the proposals in this Budget are aimed at clarifying the law to provide certainty of treatment and to safeguard tax revenues.

Exemptions and Allowances

Income tax exemption thresholds

The income tax exemption thresholds are the level below which taxpayers do not have a liability to income tax.

The practice in recent years has been to increase the exemption thresholds by reference to the lower of the RPI figure and the annual increase in average earnings. In Budget 2012 however, exemption thresholds were increased by a higher amount to provide greater benefit to lower income taxpayers. In 2013 the exemption thresholds were increased by 3% in line with the increase in RPI for the year to 30 June 2012. This was the higher of the two figures as the increase in average earnings in the period to June 2012 was 1.5%.

The RPI at 30 June 2013 was 1.5%. The annual increase in average earnings at 30 June 2013 was 2.2%.

The Minister proposes that thresholds are increased by 1.5% in combination with a reduced marginal rate (see below).

The affected population will include all marginal relief taxpayers and a number of taxpayers that currently pay tax at the standard rate that are brought into the marginal rate as a consequence of the increase in the thresholds.

The cost of increasing the income tax exemption thresholds by 1.5% will be approximately £2.5m.

Decrease in the income tax marginal rate

The Minister proposes that the marginal rate of tax be decreased from 27% to 26%.

The affected population will include all marginal relief taxpayers and a number of taxpayers that currently pay tax at the standard rate that are brought into the marginal rate as a consequence of this proposal.

Based on data from the 2011 year of assessment, the proposal will reduce the tax liability of approximately 84% of the taxpaying population (around 40,000 households).

The cost of decreasing the marginal rate by 1% is approximately £7.8m.

The overall cost of a 1.5% increase in exemption thresholds combined with a 1% decrease in the marginal rate will be approximately £10.3m. The income tax forecasts in the MTFP have been prepared on the basis of a 3% increase in the income tax exemption thresholds only, being the estimate of the RPI at the time the forecasts were prepared. There will therefore be an increased cost over that forecast of £4.9m (£10.3m less £5.4m currently forecast).

FIGURE 1 – TAXPAYERS IN THE MARGINAL RATE BAND FOR 2011

Single persons	23,046
Single persons (aged 63+)	2,893
Married couples / civil partnerships	10,753
Married couples / civil partnerships (aged 63+)	3,048
TOTAL	**39,740**

Enhanced income tax exemption threshold for parents of children in higher education

In the 2012 Budget the Minister provided substantial additional support to working parents with young children by almost doubling the amount of child care tax relief available for pre-school children. As a result additional tax relief of approximately £1.5m is granted annually to these parents. In this budget the Minister is proposing to bring in a measure aimed at helping middle income households with children at university.

At present taxpaying parents (both marginal and “20 means 20”) with children over the age of 17 years and in full time higher education receive a tax allowance of £6,000 per child – compared to the standard child allowance of £3,000 per child. This allowance can be claimed by parents with children at university off Island or with children on Island studying qualifying university degrees. The amount of the allowance is also added to the income tax exemption thresholds therefore ensuring that marginal rate taxpayers receive benefit as well as standard rate taxpayers.

The Minister proposes to allow additional tax relief to parents by adding £3,000 per child in full time higher education to the income tax exemption threshold. The effect of increasing the tax exemption threshold rather than the higher child allowance will be to target those taxpaying parents currently within the marginal relief bracket and those parents who by virtue of the increase in the thresholds will be brought into this bracket. The majority of taxpaying parents that currently pay tax at the standard rate will not be affected.

This proposal will mean a tax reduction for those taxpaying parents currently in the marginal relief bracket and those brought within it of up to £780 per child.

The cost of the enhanced income tax exemption threshold for parents of children in higher education will be approximately £900,000.

The effects of these proposals are outlined in Figures 2 and 3.

FIGURE 2 – EXEMPTION THRESHOLDS FOR 2013 AND 2014

	2013	2014
Single Person	£13,780	£14,000
Single Person (aged 63+; 65+ for 2014 onwards)	£15,370	£15,600
Married Couple/Civil Partnership	£22,090	£22,400
Married Couple /Civil Partnership (aged 63+; 65+ for 2014 onwards)	£25,280	£25,700

FIGURE 3 – ADDITIONS TO EXEMPTION THRESHOLDS

	2013	2014
Wife / Civil Partner 'B' working	£4,500	£4,500
Child	£3,000	£3,000
Child in higher education	£6,000	£6,000
Child in higher education enhanced exemption	_	£3,000
Single Parent	£4,500	£4,500
Child care tax relief	£6,150	£6,150
Enhanced child care tax relief (pre-school age children)	£12,000	£12,000
Mortgage interest relief for a home*		

*Mortgage interest relief for homeowners is available for interest paid on mortgages up to £300,000.

Figure 4 illustrates the impact of these proposals on sample households.

FIGURE 4 – IMPACT ON SAMPLE HOUSEHOLDS

	Income	2013 liability	2014 liability	Saving
Single, no children	£20,500	£1,814	£1,690	£124
Married, 2 children, wife not working	£36,000	£2,136	£1,976	£160
Married, 2 children (1 child at university), wife working	£40,000	£1,191	£286	£905
Married, 2 children, £240k mortgage (at 5% interest), wife working	£62,000	£4,701	£4,446	£255
Married, 2 children (1 child at university), wife working	£70,000	£9,291	£8,086	£1,205
Married, 2 children (1 child at university), wife working	£140,000	£26,200	£26,200	Nil
Single pensioner	£20,500	£1,385	£1,274	£111
Married pensioner	£26,000	£194	£78	£116

Income tax allowances for standard rate taxpayers

The Minister proposes that the income tax allowances for higher earners who pay tax at the standard rate are unchanged for 2014. These allowances are shown in Figure 5.

FIGURE 5 – INCOME TAX ALLOWANCES FOR STANDARD RATE TAXPAYERS

	2013	2014
Child	£3,000	£3,000
Child in higher education	£6,000	£6,000
Single Parent	£4,500	£4,500

Tax facts

The following tax facts provide an illustration of the existing personal tax structure, and also provide relative comparisons against other jurisdictions.

The tax threshold (i.e. the point above which an individual starts to pay income tax) is determined by the individual's personal circumstances. For example, a married couple, who are both working and have two children (one at university), paying mortgage interest of £7,500, do not become liable to income tax in 2013 until their income exceeds £43,090. For 2014 this would increase to £46,400 under the current proposals. Figure 6 refers.

FIGURE 6 – INCOME TAX THRESHOLDS

	2013	2014
Married Couple Exemption	£22,090	£22,400
Wife's Earned Income (max)	£4,500	£4,500
Child Allowance	£3,000	£3,000
Child Allowance (higher)	£6,000	£6,000
Child in higher education enhanced exemption	-	£3,000
Mortgage Interest	£7,500	£7,500
Total	**£43,090**	**£46,400**

Tax Comparisons

The income tax thresholds in Jersey mean that many residents pay less tax than in most neighbouring territories. Figure 7 refers.

FIGURE 7 – COMPARISONS OF TAX PAYABLE

The income tax payable by a married couple, where both spouses are working, in 2013 with a joint income of £41,000, without children or a mortgage, is as follows:

Jersey	£3,891
Isle of Man	£2,380
Guernsey	£4,410
UK 2013/14 (based on one person having an income of £40k)	£6,312
UK 2013/14 (based on each person having an income of £20k)	£4,224

The income tax payable by married pensioners in 2013 (aged 63+) with an income of £26,000 without a mortgage, is as follows:

Jersey (wife not working) (aged 63+)	£194
Isle of Man (aged 65+)	£538
Guernsey (aged 64+)	£710
UK 2013/14 (based on one person having an income of £26k) (age 65–74)	£3,100
UK 2013/14 (based on each person having an income of £13k) (age 65–74)	£1,000

Additional Income Tax Proposals for 2014

The Minister proposes amendments to the Income Tax (Jersey) Law 1961 (“Income Tax Law”) in respect of the following:

Remove the restriction to child allowance by reference to the child’s earned income

At present a child’s income (earned and unearned) above £3,000 is taken into account when calculating both the standard and higher child allowance due to the parent. The only occasion when the child’s earned income is not taken into account is any income earned in the year of assessment after the child has completed a course in full-time higher education.

It is proposed that the restriction in the relief based on the child’s earned income is removed so that any earned income of the child is not taken into account when calculating both the standard and higher child allowances. The restriction will remain for unearned income. The cost of this proposal will be approximately £420,000.

Increase the age of entitlement for single, married persons and civil partners to the higher income tax exemption threshold

It was announced in the 2013 Budget that a proposal would be brought forward in the 2014 Budget to increase the age at which taxpayers can benefit from the higher exemption thresholds.

Currently a single person, married couple and civil partnership are entitled to a higher income tax exemption threshold if the single person, husband or wife or either of the civil partners are aged 63 years of age or over at the beginning of the income tax year of assessment.

It is proposed that the age entitlement of 63 years is increased to 65 years with effect from the year of assessment 2014.

‘Grandfathering’ provisions will be applied which will ensure that any individual who became 63 in 2012 and who receives the higher income tax exemption threshold for the year of assessment 2013 will continue to do so for the year of assessment 2014 and ensuing years. The estimated additional revenue resulting from this proposal will be approximately £750,000.

Income Tax Instalment System (ITIS) provisions – restrict credit to controlling directors

When an employer deducts tax from an employee’s salary or from a director’s fees under the ITIS provisions he is obliged within 15 days of the end of the calendar month to pay that tax over to the Comptroller. If the employer fails to pay that tax to the Comptroller the employee is protected and will receive a tax ‘credit’ under the ITIS provisions for the amount of tax deducted.

‘Controlling directors’ are equally entitled to a tax credit for the tax deducted but not paid over to the Comptroller.

If a business ceases and the company is dissolved, the Comptroller may be unable to recover all or any of the outstanding tax due under the ITIS provisions to settle both the employees' and the 'controlling directors' tax liabilities. Whilst in these circumstances the provision of a tax credit is fair and equitable for employees who have had the tax deducted from their salary, for an individual who has had control of the company and its financial affairs such a provision seems unduly generous.

The Minister proposes that the Income Tax Law is amended to ensure the provision of a tax credit in circumstances where income tax deducted has not been paid over to the Comptroller no longer applies to controlling directors. It was never the intention to allow a tax credit in the circumstance described above so this proposed amendment seeks to ensure no further tax credits are afforded to controlling directors.

Create level playing field for oil importation and distribution companies – liable to tax at 20%

The Income Tax Law was amended to tax the profits arising from the importation and supply of hydrocarbon oil at the standard rate of 20% with effect from 1 January 2012.

The legislation also provides that where a company carries on a trade of importing and supplying hydrocarbon oil (the importing company) and supplies oil to another company which is a subsidiary of, or connected with, the importing company, the profits of that other company arising from the trade of supplying hydrocarbon oil shall also be taxed at 20%.

The players in this sector operate in different ways. Some are both importers and suppliers which operate through one entity, some split their activities and some do either the importation or the supply. It was intended to subject all of these activities to tax at 20% but as drafted the law could be applied such that some escape tax which creates an unlevel playing field in the sector.

There was never an intention to discriminate in this way. It is proposed that a minor change is made to the legislation to ensure that the law operates as intended.

The Income Tax Instalment System (ITIS) – Mandatory online filing

ITIS was introduced in January 2006. It obliges employers to deduct tax from all employees and company directors receiving a salary or fee and to pay over that tax and provide the accompanying data within 15 days of the end of the calendar month to the Comptroller. Employers have the opportunity to submit their monthly returns either in a paper format or online.

The Taxes Office is promoting an e-business environment, reducing the amount of paper processed and encouraging taxpayers and employers to engage with the Office online.

It is the Comptroller's intention to move to mandatory online filing for ITIS returns in 2014.

The Comptroller may, at his discretion, allow certain organisations or employers to continue to file in paper format. These could include for example, bodies such as small charities and Non Profit Organisations or very small employers.

Lump Sum Donations – revoke 3 year rule of residence prior to making Lump Sum Donation

An individual may not make a donation qualifying for income tax relief until he has been resident in Jersey for more than three tax years. Whilst in the past this time limit may have been necessary so that the Taxes Office could be sure that an individual donor paid income tax before the Taxes Office were asked to repay that tax to a charity, the combination of changes made to the personal tax system in recent years means that this is no longer necessary.

Abolishing the time limit for new residents means that charities would be able to claim refunds of income tax on donations made by individuals regardless of how long they have been resident.

Allowing existing residents with housing licences granted under regulation 1(1)(k) to apply to be taxed under Article 135A(3A)

This proposal will allow some taxpayers who were granted a housing consent under regulation 1(1)(k) of the Housing (General Provisions) (Jersey) Regulations 1970 to be taxed under the 'new' (post July 2011) tax regime.

The tax regime in place prior to July 2011 actively encouraged these individuals to hold their businesses and investments outside of Jersey, which does not support the objective of inward investment growth. This was one of the drivers for changing the regime in 2011.

The advantage of allowing this would be the new employment and investment opportunities that could be created in Jersey by the transfer of business and investments from offshore to onshore, thereby encouraging economic growth.

This would be a discretionary regime, which requires the individual to formally apply to the Minister and to commit to pay the current minimum tax contribution of £125,000. Consideration will be given to applications that demonstrate an identifiable economic benefit to the Island through creating employment and/or other economic activity.

Guidance notes have been published alongside this Budget Statement setting out the criteria that should be satisfied for an application to be accepted.

Strengthening the law on tax relief for interest

A number of taxpayers utilise the availability of tax relief for interest incurred to inappropriately shelter their income from Jersey tax. An amendment to the interest relief rules is proposed that will give the Comptroller the power to limit the amount of interest that may be deducted where the interest incurred exceeds the amount that could reasonably be expected to be charged on a commercial basis. This power strengthens the Comptroller's ability to effectively challenge situations where the interest relief rules are being abused.

Allowable deduction on account of social security contributions revised for self employed

An individual who conducts a trade or profession is subject to pay Class 2 contributions to Social Security. The Income Tax Law provides that the individual may deduct as an expense from his business profits 52% of the Class 2 contributions (being equivalent to the 'employer's element' of the total contributions).

The Social Security Law has been amended such that with effect from 1 January 2012 Additional Class 2 contributions, above the earnings ceiling, became effective. The additional contributions are 2% on income between the Standard Earnings Limit and the Upper Earnings Limit. As a result the amount that an individual may deduct as a business expense is no longer a set amount of 52% - but varies between 52% and 65% of the contributions paid.

The Minister proposes that the Income Tax Law is amended to accommodate the changes to the Social Security Law to ensure the correct relief is available to taxpayers.

Repeal of tax credit for electronic delivery of income tax return

An amendment was made to the Income Tax Law in 2008 which provided for a deduction of £20 from the amount of tax payable by an individual if they filed their personal tax return online.

The purpose of the amendment was to encourage as many individuals as possible to file online as processing an electronic tax return is far more effective and efficient than processing a paper return.

The Taxes Office is in the process of developing an online filing facility for individuals which should be available on or before 1 January 2015.

It is now recognised that the £20 deduction is very generous and could involve a significant reduction in income tax revenue; particularly if there is a large number of taxpayers who use the facility and the deduction is applied each year. It is proposed to remove this deduction.

Changes to the Distribution Rules

A number of minor changes are proposed to the Distribution Rules introduced in the 2013 Budget to ensure that they are operating as intended. This includes measures to address the situation where a shareholder switches from the simplified basis of taxation to the calculated basis of taxation.

Launch of consultation regarding pensions

A consultation is being released alongside the Budget regarding the tax rules applying to pensions and pension schemes. The consultation document primarily consists of proposed amended legislation (which has been released for comment) which is aimed at simplifying and modernising the applicable tax rules.

In particular under the existing tax rules it is not possible for members of occupational pension schemes to draw a pension from their scheme whilst continue to work and accrue further benefits within the scheme. Broadly it is necessary for a member to “retire” before they are able to draw a pension from their scheme.

This means that the members of occupational pension schemes are ordinarily required to make a choice between working and retiring, preventing them from having the option of a “flexible retirement” where they combine working and the receipt of pension income in a way that suits their particular circumstances. It is proposed that the tax rules which prevent “flexible retirement” are removed entirely.

Subject to the findings of the consultation, it is anticipated that the amended legislation will be lodged with the States in spring 2014.

3. Goods and Services Tax Proposals

Background

The Minister proposes amendments to the Goods & Services Tax (Jersey) Law 2007 in respect of the following:

Definition of existing building – clarification and strengthening of existing policy

Current GST legislation and policy allows the zero rating of construction of new build dwellings but requires GST to be charged on building works applied to existing buildings, such as alteration, conversion, enlargement, improvement, reconstruction, repair and extension.

There is not an explicit definition of the term "existing building" in Jersey GST legislation but existing policy and publicity says that an existing building only ceases to exist when it is demolished to ground level, or if one wall is retained purely for planning reasons (or two if it is a corner site). Unless these conditions are met, the building works are standard rated works of alteration, conversion, enlargement, improvement, reconstruction, etc. and not of a zero rated construction of a new dwelling.

This proposal introduces a definition of the term "existing building" in the legislation to ensure that only the construction of new dwellings from the ground up will be eligible for the 0% rate and building services on existing residential property are subject to the 5% rate. There will be a 2 year "grandfathering" provision to allow for construction works that are in progress at 1st January 2014 and have been commenced under the former legislation to remain liable at 0%.

Input tax blocking order on white goods, carpets and similar goods supplied in zero rate dwellings

Current GST policy and practice requires developers and vendors of new dwellings zero-rate to account for GST on the sale of any "white" goods, carpets and other removable goods commonly supplied in new residential units. This proposal clarifies this position in the legislation.

Deregistration process

This proposal allows the Comptroller, taxpayers and their agents greater flexibility in agreeing the date from which GST deregistration should apply. This will overcome a difficulty created in the original drafting which limits the possible date to a current date or earlier but not later. This proposal provides greater flexibility to agree a suitable prospective deregistration date with a business.

Align the GST treatment of imported goods with domestically sourced goods

This proposal aligns the treatment of goods that have been imported by a Customs approved importer with those that have been sourced in Jersey with a recovery of the GST to ensure that both categories of goods are considered when applying the provisions which exist to apply a GST charge when goods (e.g. cars), are taken to private use or when a business deregisters for GST.

Discretionary power to the Comptroller to allow input tax claims that would otherwise be capped at 3 years

Current GST legislation places a 3 year time limit on the period for which a taxpayer may seek credit for GST that has been incurred. This exists to limit the time period during which a GST registered taxpayer may seek reimbursement of GST and effectively "caps" the period for which GST input tax credit is available.

In a limited range of circumstances, the 3 year restriction has placed otherwise compliant taxpayers at a financial disadvantage. This proposal gives the Comptroller a limited discretionary power to allow, upon application, input tax claims that would otherwise be capped.

4. Impôts Duty Proposals

Background

Each year, in advance of the Budget, the proposals for impôts duties are reviewed against the prevailing economic conditions, the Island's financial position and the States strategies on alcohol and tobacco.

The Minister's proposals for 2014 take all the above factors into account.

To help inform his decision the Minister has considered the following:

- The most recent rate of inflation.
- The tobacco and alcohol strategies.
- Informed consultation with the Council of Ministers and in particular the Ministers and Officers from Health and Social Services, Home Affairs and Economic Development.

It is proposed that the increases in duty will take effect at midnight on 31 December 2013.

The Budget proposals are set out in detail below and will raise additional revenue of approximately:

- Alcohol duties – £1,254,000
- Tobacco duties – £1,466,000
- Fuel duties – £399,000
- Vehicle Emissions Duty – £44,000

(The above amounts are the estimated additional revenue that will be collected by the Customs and Immigration Service in 2014 and do not take into account any increases already calculated as a result of the MTFP forecast).

Alcohol

Following consultation with the Council of Ministers, it is proposed to increase alcohol duty rates above the most recent rate of inflation.

Accordingly the Minister proposes the following:

- An 11% increase on spirits (£1.27 per litre)
- An 11% increase on strong beer/cider (exceeding 4.9% abv) (6p per pint)

- A 5% increase on wines (7p per bottle)
- A 5% increase on weaker beer/cider (not exceeding 4.9% abv) (2p per pint)

As a result of these Budget proposals, the forecast is that the annual duty collected on all alcohol will total £18,965,000 in 2014. This would be £463,000 more than forecast for 2014 in the MTFP, and £770,000 more than forecast for 2013 in the 2013 Budget (see Figure 13).

Tobacco

It is proposed that the policy of increasing duty on tobacco at a level above the cost of living is continued.

As a result the Minister is proposing to increase the rate of duty on all tobacco products by 11% (47p per packet of 20 king size cigarettes).

There is evidence to show that both locals and tourists are increasingly turning to duty free sources for their tobacco supplies and that this is because of the high cost of tobacco in the Island.

The Customs and Immigration Service has previously reported a significant increase in passengers attempting to import cigarettes in excess of their statutory allowance and there has been no change in this trend during 2013. The Service continues to monitor this activity and though it is having an impact on the revenue yield, at this time there is neither evidence nor intelligence to suggest that commercial quantities of cigarettes are being smuggled into the Island.

As a result of the Budget proposals, the forecast is that the annual duty collected on all tobacco will total £14,789,000 in 2014. This would be £2,976,000 more than forecast for 2014 in the MTFP and £785,000 more than forecast for 2013 in the 2013 Budget (see Figure 13).

Fuel

The Minister continues to consider all issues regarding the duty on fuel, including the current worldwide price of hydrocarbon oil and the retail price of fuel at garages in the Island.

Having taken this into account and having considered the fact that there has been no increase in fuel duty for the last 2 years and an increase of only 2p per litre over the last 5 years, it is proposed to increase fuel duty by 2% (1p per litre).

As a result of the Budget proposals, the forecast is that the annual duty collected on fuel will total £20,363,000 in 2014. This would be £1,174,000 less than forecast for 2014 in the MTFP and £772,000 less than forecast for 2013 in the 2013 Budget. The reduction is mainly due to lower levels of importation than previously forecast.

Vehicle Emissions Duty

Vehicle Emissions Duty (VED) was introduced in September 2010 with an estimated annual revenue yield of £2 million.

The number and type of new vehicles registered has not proved consistent with the original modelling used to formulate the duty banding and in 2012 the total yield for VED was approximately £840,000. It is estimated that the yield will be similar in 2013.

It is not known the extent to which the introduction of VED has influenced consumers' decisions on vehicle purchases, but the current economic situation must have also been a factor. In addition it is apparent that new vehicles are being manufactured with reduced carbon dioxide (CO^2) emission figures. As a result these vehicles are either falling into a lower revenue VED band or the band where the revenue collection is zero.

For 2014 the Minister proposes an increase of 5% to all VED bands.

As a result of the Budget proposals, the forecast is that the annual duty collected for VED will total £924,000 in 2014. This would be £76,000 less than forecast for 2014 in the MTFP and £126,000 less than forecast for 2013 in the 2013 Budget. This is mainly due to different numbers and types of vehicles being imported and registered to those originally modelled.

Detailed Duty Increases for 2014

FIGURE 8 – DUTY INCREASES PROPOSED FOR 2014

	Current Duty	Proposed Duty	Increase (rounded to the nearest penny)
Litre of whisky at 40%	£11.49	£12.76	127p (11%)
Bottle of table wine	£1.38	£1.45	7p (5%)
Pint of beer ≤ 4.9% abv	£0.33	£0.35	2p (5%)
Pint of beer > 4.9% abv	£0.51	£0.57	6p (11%)
20 King size cigarettes	£4.29	£4.76	47p (11%)
Litre of unleaded petrol	£0.43	£0.44	1p (2%)

FIGURE 9 – PROPOSED RATES OF VEHICLE EMISSIONS DUTY BASED ON CO² MASS EMISSION FIGURE

CO² mass emission figure:	LPV first registered in Jersey	LPV first registered outside Jersey 1 year or less ago	LPV first registered outside Jersey more than 1 but 2 years or less ago	LPV first registered outside Jersey more than 2 years ago
120g or less	£0	£0	£0	£0
More than 120g but not more than 150g	£46	£46	£28	£23
More than 150g but not more than 165g	£139	£139	£92	£69
More than 165g but not more than 185g	£208	£208	£133	£105
More than 185g but not more than 225g	£348	£348	£226	£174
More than 225g but not more than 250g	£695	£695	£453	£348
More than 250g but not more than 300g	£1,158	£1,158	£753	£579
More than 300g	£1,448	£1,448	£944	£723

Note: LPV means a light passenger vehicle, being a motor vehicle designed and constructed for the carriage of passengers and comprising no more than 8 seats in addition to the driver's seat.

FIGURE 10 – PROPOSED RATES OF VEHICLE EMISSIONS DUTY BASED ON CYLINDER CAPACITY OF ENGINE

Cylinder capacity of engine	Vehicle first registered in Jersey	Vehicle first registered outside Jersey 1 year or less ago	Vehicle first registered outside Jersey more than 1 but 2 years or less ago	Vehicle first registered outside Jersey more than 2 years ago
1000cc or less	£0	£0	£0	£0
More than 1000cc but not more than 1400cc	£174	£174	£116	£87
More than 1400cc but not more than 1800cc	£290	£290	£191	£145
More than 1800cc but not more than 2000cc	£440	£440	£284	£221
More than 2001cc but not more than 2500cc	£579	£579	£376	£290
More than 2501cc but not more than 3000cc	£868	£868	£568	£435
More than 3001cc but not more than 3500cc	£1,158	£1,158	£753	£579
More than 3500cc	£1,448	£1,448	£944	£723

Comparisons with neighbouring jurisdictions

FIGURE 11 – 2013 RETAIL PRICE MARGINS – COMPARISONS WITH THE UK (JUNE 2013)

	Jersey Retail Price	Jersey Duty	GST	Price net of duty & GST	Duty & GST as % of price	UK Retail Price	UK Duty	UK Vat	Price net of duty & VAT	Duty & VAT as % of price
Litre of whisky	£20.18	£11.49	£0.96	£7.73	62%	£19.00	£11.29	£3.17	£4.55	76%
Pint of standard beer	£3.79	£0.33	£0.18	£3.28	13%	£3.30	£0.49	£0.55	£2.26	31%
20 King size cigarettes	£6.80	£4.29	£0.32	£2.19	68%	£7.77	£4.68	£1.30	£1.80	77%
Litre of Unleaded Petrol	£1.23	£0.43	£0.06	£0.74	40%	£1.34	£0.58	£0.22	£0.54	60%

Note: These figures are before the impact of the Budget proposals and the prices shown are based on a narrow range of sources but are for equivalent products. There will be considerable price variations in each jurisdiction, especially for wine and beer. Fuel prices are also subject to rapid change.

The Figure below illustrates that in all of the above examples of dutiable products the proportion of price made up by duty and tax is lower in Jersey than the UK. Even allowing for other cost factors in Jersey there would still appear to be a much greater margin in the retail price of products in Jersey than exists in the UK.

FIGURE 12 – A COMPARISON OF TYPICAL 2013 TAX AND DUTY LEVELS FOR A RANGE OF COMMODITIES

	Jersey Duty	Jersey GST @ 5%	Guernsey Duty	UK Duty	UK Vat @ 20%	France Duty	France TVA @ 19.6%
Litre of Whisky @ 40%	£11.49	£0.96	£10.62	£11.29	£3.17	£5.79	£3.16
Bottle of table wine	£1.38	£0.31	£1.48	£2.00	£1.17	£0.02	£0.99
Pint of beer/lager @ 4.5% abv	£0.33	£0.18	£0.37	£0.49	£0.55	£0.16	£0.82
Pint of beer/lager @ 5.5% abv	£0.51	£0.19	£0.37	£0.60	£0.55	£0.19	£0.82
20 King size cigarettes	£4.29	£0.32	£3.48	£4.68	£1.30	£3.56	£0.80
Litre of Unleaded Petrol	£0.43	£0.06	£0.47	£0.58	£0.22	£0.53	£0.23
Litre of Diesel	£0.43	£0.06	£0.47	£0.58	£0.23	£0.38	£0.20

FIGURE 13 – SUMMARY OF DUTY REVENUES

	MTFP (July 2012)		Budget 2013 (Dec 2012)		Budget 2014 (Oct 2013)	Contribution to Budget measures 2014
	2013 £'000	2014 £'000	2013 £'000	2014 £'000	2014 £'000	2014 £'000
Impôts on Spirits	4,157	4,133	4,161	4,137	4,747	610
Impôts on Wine	7,248	7,504	7,256	7,512	7,729	217
Impôts on Cider	1,039	1,107	1,040	1,108	930	(178)
Impôts on Beer	5,732	5,758	5,738	5,764	5,559	(205)
Impôts on Tobacco	12,392	11,813	14,004	13,425	14,789	1,364
Impôts on Motor Fuel including Fuel Duty Rebate	21,221	21,537	21,135	21,451	20,363	(1,088)
Impôts on Goods Imported	150	150	150	150	150	-
Vehicle Emissions Duty	1,000	1,000	1,050	1,050	924	(126)
TOTAL IMPÔTS DUTY	**52,939**	**53,002**	**54,534**	**54,597**	**55,191**	**594**

Note: the 2013 Budget agreed increases to Impôts duties for alcohol, tobacco and VED.

FIGURE 14 – EXPLAINING THE NET VARIATION TO FORECASTS

	2014 Budget Proposals 2014 £'000	Less: Original MTFP Assumptions 2014 £'000	Changes in Volume assumptions 2014 £'000	Net variation to Forecasts 2014 £'000
Impôts on Spirits	470	(107)	247	610
Impôts on Wine	368	(184)	33	217
Impôts on Cider	65	(21)	(222)	(178)
Impôts on Beer	351	(131)	(425)	(205)
Impôts on Tobacco	1,466	(334)	232	1,364
Impôts on Motor Fuel including Fuel Duty Rebate	399	(498)	(989)	(1,088)
Vehicle Emissions Duty	44	0	(170)	(126)
TOTAL IMPÔTS DUTY	**3,163**	**(1,275)**	**(1,294)**	**594**

The table shows the estimated net variation to forecasts after allowing for the duty assumptions in the MTFP for 2014 of 2.5% and the estimated effect of the changes in the assumption for the volume of each commodity imported since the MTFP and Budget 2013 assumptions in March and September 2012.

5. Stamp Duty and Land Transaction Tax Proposal

The Minister proposes an amendment to the Stamp Duties and Fees (Jersey) Law 1998 in respect of the following:

First time buyer relief

Amongst other things, Stamp Duty (SD) is charged on transactions involving land, and on the registration of charges associated with land. Land Transactions Tax (LTT) imposes similar charges on transactions in the shares of companies which own residential dwelling accommodation.

First-time buyers are currently eligible for relief from SD and LTT in respect of transactions regarding dwelling accommodation up to a maximum of £450,000. This maximum threshold was temporarily increased from £400,000 in the 2012 Budget for a period of twelve months from 1 December 2011. The application of the increased maximum threshold was extended in the 2013 Budget to cover the period from 1 December 2012 to 31 December 2013.

The Minister proposes to extend the application of the increased maximum threshold for a further 12 months to 31 December 2014. The cost of this proposal will be approximately £300,000.

6. On-going and Future Reviews

Long term tax strategy

Following the establishment of long term tax strategy principles in the Medium Term Financial Plan 2013-2015, the Treasury is in the process of producing a detailed programme which will set out the key tax objectives to be delivered over the next 5 to 10 years. This will include, for example, a step plan and timetable to deliver the modernisation of the personal tax regime, such as self assessment and independent taxation.

The long term tax programme will be aligned with the long term tax principles and support the Strategic Plan and Economic Development Strategy. It will also incorporate the Taxes Transformation Programme.

The report will be published alongside the 2015 Budget proposals.

The on-going development of tax policy

As noted above, the main focus of tax policy in 2014 will be the development of a long term programme which will define the way forward for Jersey's tax regime. Alongside that a number of projects will continue to be progressed although these will also be incorporated into the long term programme. These will include:

- Continuation of the property tax review.
- Modernisation and simplification of the personal tax regime. Work will continue during 2014 to identify steps that can be taken in the near term to aid the modernisation and simplification programme.
- Protection of tax revenues. There will be increased focus on implementing the new company distribution rules to ensure proper compliance.

Taxes Transformation Programme

The Taxes Office is now in the second year of this major modernisation programme but since 2012 the main focus has been working with the Social Security Department to implement the new Long Term Care scheme. The Long Term Care contributions will be collected by the Taxes Office as agents on behalf of the Social Security Department.

It was announced earlier this year that the Long Term Care contributions will not start until 2015, which is a delay of one year from the original plan and is subject to States approval. The Taxes Office will continue to develop their Income Tax computer system to include Long Term Care functionality and complete all necessary preparations for the successful launch of contributions from January 2015.

The Taxes Transformation Programme has been re-scheduled as a result of developing the Long Term Care project. Notwithstanding this, certain discrete components of the transformation programme have been run in parallel.

In terms of modernisation, the Taxes Office introduced online payments from February and online submission of personal tax returns (for taxpayers using agents) from March this year.

Project components covering:

- data and information exchange;
- risk based approach to compliance; and
- organisational restructuring.

have been started and reviews will be completed before the end of 2013.

Other projects involving internal data processing and ITIS improvement were started and completed in 2013.

In 2014 the Taxes Office will continue Long Term Care work and plan to further extend the provision of online filing of personal tax returns so that all taxpayers are included on or before 1 January 2015.

2013 Budget Consultations update

International Services Entities (“ISE”)

A Green Paper was issued alongside the 2013 Budget which looked at ways of improving the transparency and equity of the fees charged to companies in the trust company business sector and their clients. The outcome of the consultation was published on 12 April 2013.

The responses to the consultation indicated that there is no clear consensus amongst trust company businesses on the best way to charge ISE fees on their sector. By a slim majority the respondents favoured retaining the current method of charging ISE fees and therefore no changes have been proposed in the 2014 Budget.

The Minister will continue to listen to feedback from the trust company business sector and if a consensus develops around a new approach to calculating the ISE fees that they pay, whilst maintaining the same amount of overall revenue collected by the Treasury, this approach can be examined in greater detail.

7. Financial & Manpower Implications

FIGURE 15 – ESTIMATED FINANCIAL IMPLICATIONS OF THE 2014 BUDGET PROPOSALS COMPARED WITH THE MTFP

Measure	Estimated 2014 Taxation Revenue (£)
Goods and Services Tax	Neutral
Impôts Duty	
Alcohol duty increases	444,000
Tobacco duty increases	1,364,000
Fuel duty increases	(1,088,000)
VED duty increases	(126,000)
Sub Total	**594,000**
These figures represent the increased/decreased revenue compared to the 2014 MTFP forecast and not the total increase revenue that will be collected on these goods by the Customs and Immigration Service in 2014 compared to 2013.	
Stamp Duty	
Extend for a further 12 months the first time buyer relief in respect of property costing between £400,000 and £450,000	(300,000)
Sub Total	**(300,000)**
Total Financial Implications 2014	**294,000**

Measure	Estimated Impact on 2015 Taxation Revenue (£)
Income Tax	
Increase Income Tax exemption thresholds by 1.5%	2,900,000*
Decrease in the Income Tax Marginal Rate from 27% to 26%	(7,800,000)
Enhanced income tax exemption threshold for parents of children in higher education	(900,000)
Remove the restriction to child allowance by reference to the child's earned income	(420,000)
Increase the age of entitlement for single, married persons and civil partners to the higher exemption threshold	750,000
Sub Total	**(5,470,000)**

The income tax measures relate to the income tax year of assessment 2014. These will impact on the tax revenues to the States in 2015. However, most current year basis taxpayers under ITIS will see the benefit of these measures during 2014. This is because the measures will impact on the calculation of their provisional ITIS effective rate.

* Note: this is an updated figure after allowing for the most recent tax data (YOA 2011).

Manpower Implications

The proposals within the Budget Statement 2014 will be implemented without any increase to current approved staffing levels.

PART C – CENTRAL GROWTH ALLOCATION

8. Central Growth Allocation 2014

Proposals for the Allocation of Growth for 2014

In the debate of the Medium Term Financial Plan (MTFP P69/2012) in November 2012, the States agreed an amendment by the Chief Minister to the proposals by the Corporate Services Scrutiny Panel for a central growth allocation in 2014 and 2015.

The amendment by the Chief Minister resulted from a review by Ministers of those growth bids which could be held centrally and allocated in future years' annual Budget.

The Council of Ministers is proposing that the Allocation of Central Growth for 2014 of £2,210,000 and associated funding of £1,460,000 for 2015 be allocated to departments in line with the original allocation.

The Treasury has confirmed with departments that these allocations are still a priority and that funding is required from 2014 onwards. If the proposals are agreed by the States the individual department spending limits will increase in 2014 and 2015 by the amounts shown in the Table below.

This Table shows the growth schemes which make up the proposals for the allocation of central growth to departments for 2014 and 2015. Each of these schemes is described overleaf.

FIGURE 16 – PROPOSED CENTRAL GROWTH ALLOCATION 2014 AND 2015

	Proposed Allocations to Departments from Central Growth Allocation in 2014 and 2015	Dept	2013 £'000	2014 £'000	2015 £'000
33	External Relations: International meetings, monitoring and visiting dignitaries	CMD	0	160	160
34	External Relations: External specialist advice	CMD	0	100	100
52	Fund permanent members of the CSR delivery team	CMD	0	150	150
			0	410	410
43	Marine Response Team	HA	0	25	25
43a	Increased running costs of new prison facilities	HA	0	25	25
18	Private Sector Rental Support	SSD	0	750	1,000
49	Treatment and disposal of ash	TTS	0	1,000	0
	Total		**0**	**2,210**	**1,460**

Note: The allocation to Home Affairs was originally a single allocation of £50,000 to the Marine Incident Response Group (MIRG).

33. External Relations: International meetings, Monitoring and visitors Dignitaries – (CMD) - £160,000 from 2014

External Relations was established using non-recurring funding sources. During 2010 and 2011 this cost was met from Fiscal Stimulus. This budget has been reduced from £260,000 in 2011 after agreeing joint monitoring contracts with Guernsey from 2012 onwards, closing the London office space used previously by the Director International Finance and cancelling the Paris monitoring contract. Whilst there is now a recurring budget for the 6 core staff and office expenses, the international operations programme is not funded. The international operations programme requires a recurring budget of £160,000 from 2014.

34. External Relations: External specialist advice (CMD) – £100,000 from 2014

Since its establishment with non-recurring funding, External Relations has needed to commission specialist technical advice. Currently, technical expert advice from the London School of Economics Trade Policy Unit is required, for example, on the extension of the UK membership of the World Trade Organisation to include Jersey. £100,000 will buy on average 2 to 3 specialist reports per annum and recurring funding is required from 2014.

52. CSR: Fund permanent members of the CSR delivery team – (CMD) - £150,000 from 2014

This team previously undertook the role of CSR Delivery Team but has now become the PSR Programme Office. The budget for the two members of staff was funded from the Restructuring Provision during the CSR process (2011-13) but now requires permanent funding of £150,000 from 2014 to support the Public Sector Reform programme. It is anticipated that this may need to be supplemented with additional temporary resource as required.

43. Marine Response Team (MRT) – (HA) - £25,000 from 2014

The funding for a UK Maritime off-shore ship firefighting capability has not been re-instated by either the UK Department for Transport or the Department of Communities and Local Government. There remains no UK provision to assist with emergency firefighting, industrial accidents or chemical incidents at sea. Many UK Fire and Rescue Services and their Authorities with notable maritime risk have taken the decision to fund the shortfall in order to maintain such a capability in and around their coastal waters.

The States of Jersey Fire and Rescue Service has developed and implemented a comprehensive local Marine Response Strategy, supported by capability, tactics and operations. These have been incorporated into Jersey Coastguard and Condor Marine Services Emergency Response Plan.

Central Growth allocation is required in order that the States of Jersey Fire and Rescue Service can maintain its capability to deal with fires, chemical release or industrial accidents on a vessel in Channel Island waters. This will also enable Jersey Fire and Rescue Service to access mutual assistance from those Services that have a maritime response capability, if required.

43a. Increased Running Costs of New Prison Facilities – (HA) - £25,000 from 2014

The prison was designed in the late 1960s and was opened in 1974. A programmed redevelopment (Masterplan) commenced in 2003 to address some of the prison estate's shortcomings which were reinforced in previous inspections. The first five phases of the Masterplan have been delivered or are currently on site.

The construction of a new visitors room and staff facility (phase four) opened in April 2013 and construction work on a new stores and engineers' facility (phase five) commenced in May 2013 with a target completion date of February 2014. In addition, a new classroom, boiler house and greenhouse have now been constructed in the horticultural area of the prison.

These new facilities have increased the running costs of the prison which cannot be accommodated within the Home Affairs Department's net revenue expenditure.

18. Private Sector Rental Support – (SSD) - £750,000 in 2014 and £1.0 million from 2015

One impact of the proposed Housing incorporation and subsequent adjustment to social housing rental will be a likely knock on effect in private sector social housing rents. The effect of increased income support due to these rent increases will be recovered from both the new housing association and existing housing trusts. However, there will be an increase to those private sector social housing rents through income support which will not be recoverable. This could be in the order of £1 million. The increase in housing rents to 90% of market value is proposed to be introduced from April 2014.

49. Treatment and disposal of incinerator ash – (TTS) - £1,000,000 in 2014

Currently bottom and fly ash (APC residue) are disposed of in fully lined ash pits built to a specification to store the hazardous and non hazardous ash. There is increasing pressure to find sustainable methods for disposal or recycling of both bottom and fly ash. These pressures will require investment in new infrastructure in order to implement alternative disposal / recycling methods which will also increase the life of La Collette.

PART D – PROGRAMME OF CAPITAL PROJECTS

9. Capital Programme 2014

Introduction

The Medium Term Financial Plan (MTFP) set out the capital programme for each of the years 2013–2015 and the debate on the MTFP approved the capital programme, in total, for each of these years. The budget for each of these years will approve the detailed list of projects. To comply with the Public Finances (Jersey) Law 2005, therefore, the States is asked to approve the detailed list of capital projects for 2014.

The MTFP approved a total allocation in 2014 of £88,892,000. The review of the proposed programme has identified a reduced cost for the additional primary school accommodation and future hospital planning. It is proposed that this variance is used to accommodate an additional allocation for TTS in respect of works at Green Street Car Park, ESC for work required to meet their Sports Strategy and an additional allocation for Fiscal Stimulus and Parish Projects. Allocations have also been included for the initial phases of the Future Hospital Project and Liquid Waste Strategy.

A summary of the capital expenditure proposals for the departments is shown below and also at Summary Table D.

FIGURE 17 – CAPITAL PROGRAMME 2014

Capital Programme 2014	£'000 2014 Budget
Chief Minister's	
Web Development	170
JDE Development & Upgrade	370
Application remediation Windows 8	500
Chief Minister's total	**1,040**
Education, Sport and Culture	
School ICT	1,000
Autism Support Unit	1,066
FB Fields Running Track	810
Les Quennevais Artificial Pitch	650
St James Centre	2,500
Additional Primary School Accommodation (Phase 1)	8,188
Sports Strategy Infrastructure (Phase 1)	1,550
Education, Sport and Culture total	**15,764**
Department of the Environment	
Fisheries Vessels	100
Met Radar Refurbishment/ Upgrade	350
Countryside Infrastructure	200
Department of the Environment total	**650**
Health & Social Services	
Future Hospital (Phase 1)	10,200
Main Theatres Project	1,837
Future Hospital – planning	500
Integrated Assessment and Intermediate Care	500
Refurbishment of Sandybrook	1,700
Health & Social Services total	**14,737**
Home Affairs	
Police Station Relocation - Tranche 4	1,000
Home Affairs total	**1,000**
Transport and Technical Services	
Infrastructure Rolling Vote	6,657
Refurbishment of Clinical Waste Incinerator	300
Liquid Waste Strategy (Phase 1)	10,100
Ash Cells & La Collette Headland	1,051
New Public Recycling Centre	2,050

Capital Programme 2014	£'000 2014 Budget
Bottom Ash Recycling	1,538
Scrap Yard Capital Basic Infrastructure	1,025
EFW Plant La Collette Replacement Assets	1,586
Project - Green Street Car Park	1,500
Transport and Technical Services total	**25,807**
Treasury & Resources (inc. JPH)	
Tax Transformation Programme & IT systems	500
Demolition of Fort Regent Pool	750
Fiscal Stimulus and Parish Projects	1,252
Treasury & Resources (inc. JPH) total	**2,502**
Vehicle replacement (additional from consolidated fund)	**1,500**
Replacement assets	**3,692**
Total Projects – Capital Allocation	**66,692**
Housing	
Social Housing Programme	22,200
Total Programme	**88,892**

Chief Ministers Department

Web Development (£170,000 for 2014). The States web sites (including the intranet) require on-going enhancement; in 2014 we will replace a number of ageing sites that predate the 2009 content management system standardisation. Several sites developed since 2009 will receive a refresh to reflect the increased use of mobile devices, following on from work to redesign www.gov.je in 2013.

JDE Development & Upgrade (£370,000 for 2014). The States Enterprise Resource Planning (ERP) system, JD Edwards, will be 12 years old in 2014. If the States is to renew this asset (purchased in 2000, implemented in 2002), then an upgrade programme will need to be initiated between 2014 and 2016. It is anticipated that this re-implementation of ERP will take a number of years to complete.

Application Remediation Windows 8 (£500,000 for 2014). Over the next few years the States of Jersey needs to continually invest in ensuring that the corporate desktop infrastructure is up-to-date if it is to achieve its departmental and States strategic objectives in providing an efficient government. This provision is dependent on the applications being able to function correctly.

Education, Sport and Culture

School ICT (£1,000,000 for 2014). The IT skills strategy is currently being finalised to inspire the next generation to be digital champions, confident and able in a challenging business world where IT is increasingly at the forefront. The strategy will be launched on 11th October 2013. This money is necessary to provide the infrastructure and devices to enable students to learn anytime, anyplace and also to equip the teachers with the skills necessary to harness the maximum benefit from mobile technology. £1,000,000 is shown in the indicative programme for each of the year's 2013 to 2015 making the overall total £3,000,000 for School ICT project.

Autism Support Unit (£1,066,000 for 2014). This will be a new Autistic Spectrum Disorder unit based at Haute Vallee school including kitchen/social room, 3 smaller rooms, art store and toilets totalling 214m² as an extension to the Arts building.

FB Fields Running Track (£810,000 for 2014). To replace the running track surface which was installed in 1986 and refurbished in 1996 and to upgrade the field event facilities and netball court surface. To move the long jump/triple jump runway outside of the arena area to comply with UK Athletics Class "A" Certification to allow Island Games Competition to go ahead in 2015 and to upgrade the changing facilities at FB fields.

Les Quennevais Artificial Pitch (£650,000 for 2014). Recent studies have shown the pitch will require replacement by 2014 due to wear and drainage issues. Continued use of the pitch will see degradation of the surface increasing the likelihood of accidents or injury to users. This project is to remove the synthetic carpet and support materials and replace with new synthetic carpet.

St James Centre (£2,500,000 for 2014). It is proposed the existing Youth Service premises at La Motte Street should be sold for private development, and that part of the proceeds should be allocated for the conversion of the existing buildings in the St James complex (Church, Vicarage and School) to provide facilities for young people and the headquarters for the Jersey Youth Service. The facilities will include a canteen, offices, music studio/rehearsal rooms, and performance venue, as well as headquarters for the Prince's Trust and the Duke of Edinburgh award. The performance venue (St. James Church) will also be available for theatre groups and other cultural events, although the Youth Service will have first call on this space for use by youth groups.

Additional Primary School Accommodation (£8,188,000 for 2014). Latest information on primary demographics indicates a significant increase in pupil numbers over the next few years. As a result it will be necessary to provide increased facilities for the schooling of these students. Feasibility studies have been completed to review the options which essentially are the provision of a new school (at least 2 form entry) or the provision of additional classrooms on existing sites. Both these options have been evaluated, and the favoured option is additional classrooms on existing facilities both on a cost and educational aspect, and also due to the lack of States ownership of land on which a new school could be built in the town area. Final costings for this option are currently being undertaken – initial work has reduced the current requirement from £15,000,000 to £8,188,000 in 2014 and £2,134,000 in 2015 based on the revised scheme.

Sports Strategy Infrastructure (£1,550,000 for 2014). This will be used on a series of projects at a number of sporting venues around the Island identified as those which best meet the needs identified in the Sport Strategy Green Paper following consultation. Projects include but are not limited to; artificial grass pitches at school sites, tennis court resurfacing, Les Quennevais cycle track resurfacing. Part of this funding will contribute towards the refurbishment of sport centres. Particular consideration will be given to ensuring facilities are ready for Natwest Island Games in 2015. A further £1,450,000 will be required in 2015 for the next phase of work.

Department of the Environment

Fisheries Vessels (£100,000 for 2014). The fisheries vessel the Norman Le Brocq has an asset life of 10 years; however, it is due a refurbishment every 5. This £100,000 will fund the mid life refurbishment of the vessel before it is replaced in 2019.

Met Radar Refurbishment/Upgrade (£350,000 for 2014). This project is to refurbish the Met Radar in order to extend the life of the existing asset and therefore delay the planned upgrade until 2024.

Countryside Infrastructure (£200,000 for 2014). The resources are insufficient to adequately maintain the national park and environmental car parks. There is also a need to invest in additional infrastructure, e.g. footpaths. This would enable an improvement to the network for walking and encourage people to live a healthier lifestyle.

Health and Social Services

Future Hospital (Phase 1) (Design Development, Preliminary Works and Transitional Capacity Requirements) (£10,200,000 for 2014). This funding provides for preliminary activities that are required to enable the phased main works programme to be undertaken.

The funding will also enable the acquisition of land necessary to complete site assembly for the proposed developments and for the project team to undertake design works for the initial phases and carry out some required necessary preliminary works.

This funding stream will also address the transitional capacity shortfall in bed numbers available in the general hospital before future hospital capacity can be provided. The funding will support the cost of providing the most appropriate transitional capacity to enable non acute patients to be rehabilitated or provided with supported care in the community.

Main Theatres Project (£1,837,000 for 2014). This funding is the final tranche for a project designed to deliver improved theatre facilities for the hospital. In particular ultra clean laminar flow ventilation will be installed in additional theatres, and all existing air handling plant will be replaced.

It is also intended that this project addresses transitional capacity issues for the hospital in terms of theatre space which will contribute to reducing waiting times and improving the experience for patients. Overall the project will provide a total of six theatres of which four will have laminar flow.

Future Hospital – Planning (£500,000 for 2014). This funding will provide for costs associated with the professional support necessary to develop the project masterplan and progress the feasibility study for consideration by States Members in autumn 2015.

Integrated Assessment and Intermediate Care (£500,000 for 2014). This project proposes the establishment of an integrated assessment and intermediate care centre which will serve as the base for integrated adult community services (including health & social care) for the benefit of our adult population. Having the appropriate teams providing assessment and care from a single base will result in improved response times and reduce duplication. There is significant evidence that early intervention:

- results in faster recovery from illness;
- reduces unnecessary acute hospital admission;
- prevents premature admission to long-term residential care;
- supports timely discharge from hospital; and
- maximises independent living.

This project will provide an improved day care facility for those with dementia and a location for the integrated assessment and intermediate care service in order to create a single point of referral for adult services.

Refurbishment of Sandybrook (£1,700,000 for 2014). Sandybrook is a 28 bed facility adjacent to the Sandybrook day centre. It was built in 1999 and has not been refurbished since. Sandybrook provides nursing care for older people who have been assessed as needing continuing care. It was originally built as a residential home but now provides nursing care to meet a higher level of care needs. The environment is outdated and not suited to the current highly dependent residents.

The aim of the project is to:

- Update the facilities to modern care standards and adapt them for the current care needs;

- Replace and update equipment such as specialist bathroom and infection control measures; and

- Install a backup generator.

Home Affairs

Police Station Relocation – Tranche 4 (£1,000,000 for 2014). This is a continuation of funding that was initially identified in the 2012 Business Plan. £1,000,000 was approved in 2013.

Transport and Technical Services

Infrastructure Rolling Vote (£6,657,000 for 2014). The infrastructure rolling vote is designed to allow TTS to facilitate the maintenance and further improvement of the Island's infrastructure network. The allocation is split broadly between highways (34%), traffic improvements/street lighting (11%), drainage infrastructure maintenance including pumping stations (46%) and other infrastructure assets (9%). The allocation was reduced by £4,000,000 to £6,657,000 to contribute towards the funding requirements of the Liquid Waste Strategy.

Refurbishment of Clinical Waste Incinerator (£300,000 for 2014). The existing Clinical Waste Incinerator (CWI) was commissioned in 1997 with emission control and operational technology to safely deal with the risks associated with Clinical Waste. The Clinical Waste Incinerator is the only one on the Island and provides specialist high temperature incineration for hazardous clinical waste.

As the Liquid Waste Strategy (LWS) has developed, the site currently occupied by the CWI has been identified as necessary for the construction of any new Sewage Treatment Works. As such, replacing the CWI is seen as the best option and will be undertaken as part of the overall Sewage Treatment Works project.

The funding allocated in 2013 (£700,000) and 2014 (£300,000) will provide for temporary maintenance to keep the plant operating until additional funding is available as part of the LWS funding. This funding should also provide for feasibility studies and site investigations into the new Clinical Waste Incinerator.

Liquid Waste Strategy (Phase 1) (£10,100,000 for 2014). Sewage Treatment Works (£3,100,000). The liquid waste strategy is the master plan for the complete regeneration of the Bellozanne site. The sewage treatment works is the second phase of regenerating this area after the sludge project. Anticipated work includes moving to a carbonaceous plant, refurbishing the inlet works, and moving the primary and final settlement tanks. This is the first phase of the works and will encompass initial feasibility, environmental impact assessment, site investigations and service diversions.

Clinical Waste Incinerator (£7,000,000). The Clinical Waste Incinerator is now past its useful life and is located in the middle of the proposed new Sewage Treatment Works site. The project to relocate and update the technology used in the Clinical Waste process will provide for a new plant and release the necessary space at Bellozanne to enable the new Sewage Treatment Works construction to commence.

Ash Cells & La Collette Headland (£1,051,000 for 2014). The current ash cell provides a repository for ash that is safe and sustainable in the context of its proximity to the nearby Ramsar site. Ongoing revenue implications include monitoring and leachate extraction. The project brief is that the design of the cell is robust and durable and integrates with the long term La Collette Headland Plan. The La Collette Headland Plan provides an ongoing repository for the ash by-products of the new Energy From Waste (EFW) plant for the design life of the plant. Revenue implications and project brief are the same as for the existing cell, but additionally, the completed headland will enhance the completed La Collette Reclamation aesthetically, environmentally and financially. £1,025,000 was approved in 2013 and a further £1,077,000 has been identified for 2015.

New Public Recycling Centre (£2,050,000 for 2014). This project is to design and build a new, permanent Re-use and Recycling Centre for the general public. The facility would provide a one-stop reception for domestic customers to drop off the full range of recyclable materials including green waste and other residual waste. The location is yet to be finalised as the current provision at Bellozanne will need to be moved to accommodate the Liquid Waste Strategy.

Bottom Ash Recycling (£1,538,000 for 2014). This project represents a marked departure from the current policy of entombment. The recycled material has the potential to be used in a number of different ways, including a cement replacement product, a bulking agent in asphalt and a building aggregate.

TTS are currently undertaking feasibility studies into setting up an Incinerator Bottom Ash conditioning facility, consisting of complete metal separation, regrinding and conditioning. The feasibility study is due for completion during quarter 3, 2013 and will drive the exact nature of this facility. The feasibility study should finalise the exact nature and costs of this facility.

Scrap Yard Capital Basic Infrastructure (£1,025,000 for 2014). The current scrap yard is leased out by TTS. However, the former site at Bellozanne does not meet environmental regulations and a new alternative needs to be identified and constructed. Various new sites are currently being considered and the development is due to commence in 2014.

EFW Plant La Collette Replacement Assets (£1,586,000 for 2014). The EFW begun operations in October 2010 and is of strategic importance to the island. The asset must be maintained to a high level to ensure that it can handle the Islands waste, maintain electrical generation and minimise the use of chemicals and utilities. The main financial benefits stemming from the replacement of these assets include lower operating and maintenance costs and preservation of the current level of service provided to the user. As the plant is a pressure system it must be maintained to an acceptable standard to satisfy the insurance inspector. The plant must continue to be able to meet its environmental emission standards as specified in its Waste Management Licence. The plant is of strategic importance for managing the treatment of the island's waste. A long term breakdown of the plant would be difficult and expensive to deal with so would constitute an unacceptable risk. The plant also has to comply with the Waste Incinerator Directive (WID). Thus it is essential that the plant's emissions are maintained to internationally recognised safe levels.

Project – Green Street Car Park (£1,500,000 for 2014). There is a requirement to provide an additional floor of parking at Green Street Car Park as a result of the spaces that will be displaced from the Police Headquarters project. This project will provide approximately 64 spaces to compensate in part for the displaced 91 spaces.

Treasury & Resources

Tax Transformation Programme & IT Systems (£500,000 for 2014). This project is intended to implement a "Procure to Pay" purchasing system, and develop the Income Tax IT system as required by the Tax Transformation Programme.

Demolition of Fort Regent Pool (£750,000 for 2014). The pool has remained unused since December 2003. As a result, it has fallen into a poor state of repair and has become unsightly, a problem that is exacerbated by its prominent position.

Fiscal Stimulus and Parish Projects (£1,252,000 for 2014). There will be a number of small individual schemes that will have an early commencement in 2014 and that will provide fiscal stimulus and support to Parish Projects.

Other Capital

Replacement Assets (£3,692,000 for 2014). Departments go through a process of identifying those assets that are due for replacement and then conduct a prioritisation exercise to come to their final request.

Replacement Assets	£'000
Health and Social Services	2,789
Home Affairs	200
Transport and Technical Services	633
Non Minsterial	70
Total	**3,692**

Vehicle Replacement (£1,500,000 for 2014). This funding is to support the work of Jersey Fleet Management in the purchase of vehicles on behalf of departments. This is a continuation of the funding established in the 2012 Business Plan to enable the initial purchase of additional vehicles. This funding will continue to 2015 when it is assumed that the overall work of Jersey Fleet Management will be self funding.

Housing Programme

Social Housing Programme (£22,200,000 for 2014). "House our Community" is a key strategic priority for the States and has at its heart the aim that all Island residents should be housed adequately.
A detailed plan of new build sites has been prepared by the Housing Department to the end of 2019. Thereafter, it is anticipated that an allowance of £3 million per annum will be sufficient for the remaining requirements which are likely to be for life long homes.

Housing has identified a number of factors that could affect the delivery of the programme:-

- Having the capacity and access to funding to build new homes.
- A key partnership with Jersey Development Company to help deliver developments of a more challenging nature such as the development of La Collette.
- The ability to build new homes on existing sites.
- A target of 1,000 new social rented homes delivered in the next 12 years.
- An additional 100 units built for sale.

The Housing Transformation project is likely to impact 2014 in terms of timing, funding and the treatment of these projects and their inclusion within future Budgets.

States Trading Operations

For 2014, States Trading Operations comprise Jersey Harbours and Jersey Airport as part of the Economic Development department and Jersey Car Parking and Jersey Fleet Management in the Transport and Technical Services department. A summary of the capital expenditure proposals for the States Trading operation is shown below and also at Summary Table E.

	2014 Budget £
Minor Capital Assets	331,000
Jersey Airport	**331,000**
Minor Capital Assets	368,000
Jersey Harbours	**368,000**
Car Park Maintenance and Refurbishment	561,000
Jersey Car Parking	**561,000**
Vehicle and Plant Replacement	1,091,000
Jersey Fleet Management	**1,091,000**

PART E – THE ECONOMIC CONTEXT

10. The Economic Context

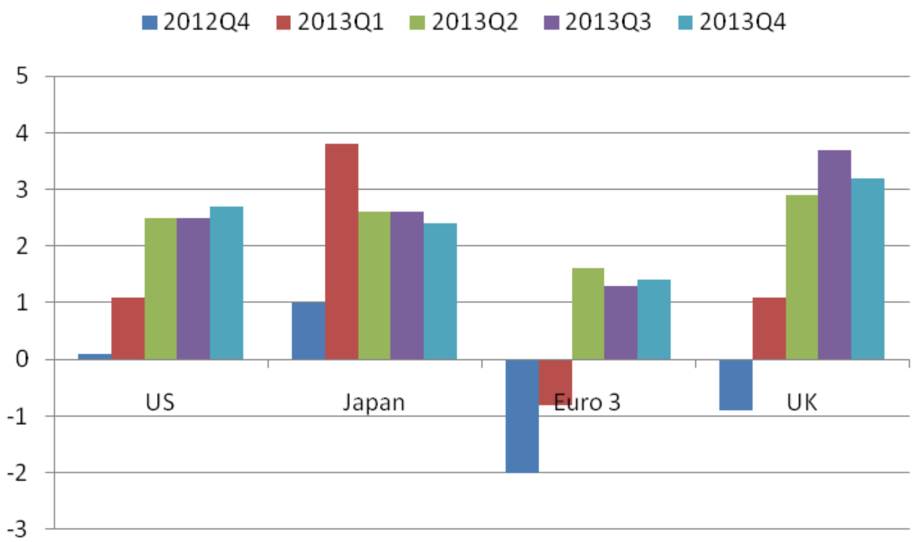
Global outlook

There have been some positive economic developments at the global level in recent months. The OECD has stated that "the pace of recovery in the major advanced economies improved in the second quarter" and that "activity is expanding at encouraging rates in North America, Japan and the United Kingdom, while the euro area as a whole is no longer in recession." However, they also note that growth has slowed in several emerging economies. They conclude that while recent improvements are welcome "a sustainable recovery is not yet firmly established and important risks remain".

The OECD expect that the improvements in growth seen in the first half of 2013 will be maintained for the rest of the year. The chart below shows that higher GDP growth rates will be maintained for the remainder of the year.

FIGURE 18 – GROWTH TRENDS IN THE KEY ECONOMIES

annnualised % change in real GDP



Euro 3 = weighted average of Germany, France and Italy

Source: OECD Interim Economic Assessment, September 2013

The OECD emphasises that risks remain high. Namely:

- The euro area remains vulnerable to renewed financial, banking and sovereign debt tensions.
- Uncertainty about the fiscal outlook and the potential withdrawal of quantitative easing clouds the outlook for the US.
- Further financial market volatility could continue to act as a drag on emerging markets.

The OECD policy advice at the global level is to continue to support demand in order to reduce the risk that the recovery will be derailed.

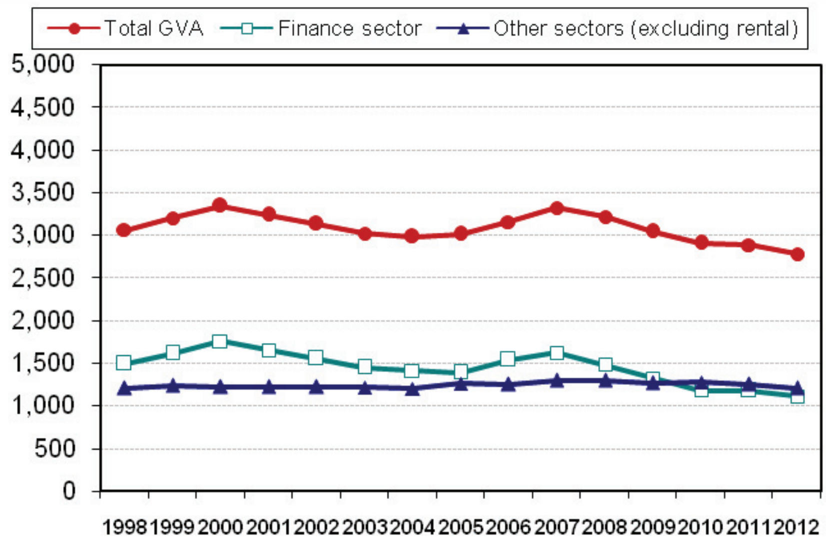
In the UK, the Bank of England has stated that a recovery appears to be taking place but that it will remain weak given the continuing post financial crisis process of adjustment and repair. With this in mind and under the stewardship of the new Governor Mark Carney, the Monetary Policy Committee has adopted a new approach to monetary policy, providing explicit guidance regarding the future conduct of monetary policy. That is, that it intends "at a minimum to maintain the present highly stimulative stance of monetary policy until economic slack has been substantially reduced, provided this does not entail material risks to price stability or financial stability". A key consideration will be the unemployment rate and whether it has fallen below 7%.

Jersey trends

In 2012, economic activity in Jersey fell by 4 per cent in real terms, representing the fifth consecutive annual fall. Although the rate of decline was slightly faster than 2011 it was only just outside the forecast of the FPP that growth would be in the region of 1 to -3% last year. The overall fall was a result of declines of -5% for the financial services sector and -4% for the non-finance sectors. Although GVA per capital fell in Jersey in 2012 to £36,700 it was about two-thirds greater than that in the UK of £21,900.

FIGURE 19 – TRENDS IN JERSEY ECONOMIC ACTIVITY

real GVA 2003 prices, £m

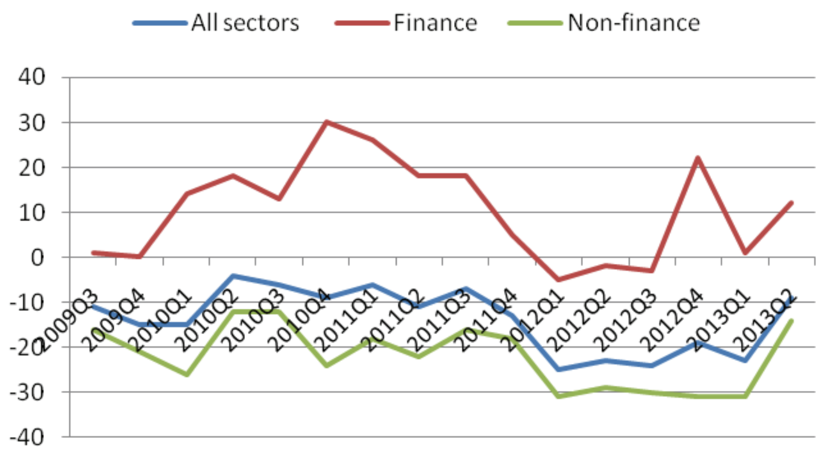


Source: States of Jersey Statistics Unit

The latest survey information for the second quarter of 2013 shows that firms report business activity is improving in the finance sector and that while it remains negative for non-finance sector, it is the least negative since September 2010 (see chart below). The headline business activity indicator remains negative in 2013Q2 but it is the least negative since September 2011. Five of the ten indicators for the finance sector improved and 7 of the 10 indicators for the non-finance sector also improved in the second quarter (although all remained negative in the non-finance sector).

FIGURE 20 – LATEST TRENDS IN ECONOMIC ACTIVITY

% balance of respondents, business activity indicator

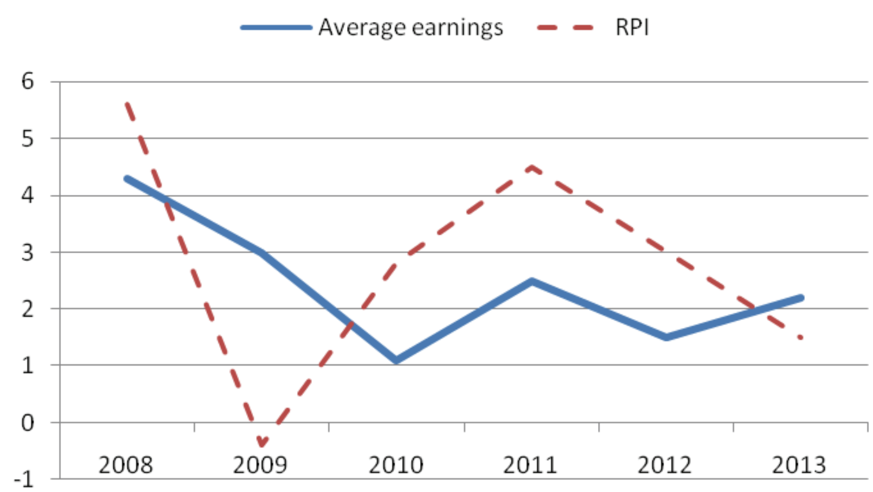


Source: States of Jersey Statistics Unit

Recent labour market data for Jersey has been more positive. In particular, real earnings have increased for the first time in four years (see chart below). Average earnings growth in June 2013 was 2.2%, 0.7% higher than in June 2012 and also than inflation. This is an early indication that economic trends in 2013 have changed significantly relative to those in 2012 when average earnings growth was 1.5% less than RPI. However, unemployment reached a peak in early 2013 and has since remained stubbornly high. Whilst 2012 saw total employment fall slightly from the record highs of 2011, the overall figure masks an increase in part-time employment at the expense of full-time employment.

FIGURE 21 – EARNINGS AND INFLATION

% change in average earnings and RPI, June each year



Source: States of Jersey Statistics Unit

Fiscal Policy Panel

The Fiscal Policy Panel (FPP) in their 2012 annual report (published in October 2012) forecast further declines in GVA in both 2012 and 2013 – of between 1 per cent and 3 per cent – with risks remaining to the downside. This represented a downgrade from their previous forecast, on the basis of the continued deterioration in the economic situation within the Island and externally, and sluggish demand as a result of fiscal constraints in many of the advanced economies.

The FPP provide important independent advice for the planning of our finances. Each year they publish an annual report containing an updated economic outlook for Jersey and advice to help with fiscal planning. Their next report is due to be published in early November.

Last year, in the context of a slightly downgraded economic outlook for Jersey in 2012 and 2013, the FPP highlighted seven key recommendations:

1. *The Panel's assessment of the economic outlook for the Jersey economy has been downgraded for 2012 and 2013 and there are indications that significant spare capacity will remain in the economy over this period. This leads the Panel to advise that the States should act now to give discretionary fiscal support to the economy in 2012 and 2013 and if practical to a greater extent than set out in the MTFP.*

2. *While the consideration of additional discretionary stimulus should not be limited purely to capital expenditure it is clear that with such significant capital allocations over the life of the MTFP consideration could be given as to whether, in a timely, temporary and targeted manner:*

    - *capital allocations in 2012 and 2013 can be spent in the year of allocation;*
    - *capital allocations from 2014 and 2015 can be brought forward to 2012 and 2013; and*
    - *unspent allocations in 2012 from previous years can be spent as quickly as possible in late 2012 and 2013.*

3. *The extent of stimulus should not be limited by the balances on the Consolidated or Stabilisation Funds. The States should give consideration as to the best way to fund needed stimulus if it is constrained by the availability of funding from these sources, not least because any constraint would be one of cash flow and funds could be repaid from future revenue.*

4. *It is too early to judge whether the stimulus that will be provided to the economy in 2014 and 2015 by capital expenditure financed by one-off receipts will be warranted but contingency plans should be made as to what measures could be implemented to reduce the extent of the stimulus if economic conditions merit such an approach.*

5. *No transfers into the Stabilisation Fund are recommended in 2012 or 2013. However, further consideration needs to be given as to how the Stabilisation Fund will be rebuilt through countercyclical fiscal policy, once the economy begins to recover. The Panel does not recommend a transfer into or out of the Strategic Reserve at this stage.*

6. *The Panel cannot rule out that there is an underlying structural imbalance between expenditure and revenue. The Panel's view is that further analysis is required by the Treasury and Resources Department to consider the nature of proposed capital expenditure, the way it is funded and what it implies for the underlying position of States' finances. If this analysis suggests there is a structural deficit then consideration should be given to its extent and nature, including a more detailed plan of action to rectify it.*

7. *The Panel have had to make significant adjustments to the financial forecasts presented in the MTFP to try to assess the underlying economic impact of the proposals. In future the presentation of States' finances would be more informative, leading to a better informed policy debate, if these types of adjustments were already included in the analysis accompanying any proposals in the MTFP or Budget.*

The 2014 Budget

This Budget is framed against the international backdrop, local economic developments and the advice of the FPP. It supports our key economic objectives of supporting the economy in the short-term through fiscal stimulus, creating new employment opportunities and laying the foundations for economic growth whilst committing to essential investment in our infrastructure.

As the OECD advise continued support at the global level and the Bank of England embark on new forward guidance, the FPP have also indicated that we should be giving discretionary support to the Jersey economy.

Budget 2014 allocates significant capital investment in 2014 totalling over £90m including:

- over £15m in education including significant investment in new primary school accommodation;
- £15m in health including upgrading main theatres;
- £25m in our transport and wider infrastructure from roads to sewage treatment; and
- over £20m in social housing.

In addition the capital programme in 2014 will be managed to try and deliver these projects in a manner which meets the FPP's 3Ts – timely, temporary and targeted. These projects are essential investment in their own right that will bring with them their own economic benefits but will be managed in such a way to maximise the support for the economy and help maintain and create employment opportunities at a time when they are most needed. Current survey evidence suggests the construction businesses in the Island have significant spare capacity – in June 2013 nearly 50% of construction businesses indicated that they were operating below capacity. In addition, a net balance of -18% of construction firms stated that there were likely to reduce employment in coming months.

At a time when unemployment remains at high levels, it is vital that the public sector does what it can to support the economy, particularly when private sector activity may take time to recover. Budget 2014 goes further than providing stimulus in the short-term and continues to provide support for the key policy areas of Back to Work and the Economic Growth and Diversification Strategy. Back to Work will help to minimise the costs to both the individual and society of the current levels of unemployment and ensure we do everything we can to get those out of work, particularly the young back into employment as quickly as possible.

We must build for the future and lay the foundations for economic growth now which will benefit us in the future. Budget 2014 cements the support for the Economic Growth and Diversification Strategy in all the 4 key areas including the new £5m Innovation Fund, supporting the continued growth and diversification of the financial services sector and a new enterprise strategy that will deliver new high value and high growth business and raise the productivity of the whole economy.

The Minister for Social Security has already published a report in August on the new Long Term Care scheme that will help Islanders pay for care, either in their own home or in a care home. If the States agree, the new long-term care scheme will start in July 2014, offering greater protection for hard working Jersey families. However, although the benefits from the scheme would be available from next year, contributions to the scheme would not begin until 2015 at 0.5% of taxable income, rising to 1% in 2016. To prevent money being taken out of the economy while it is still under pressure, the Treasury has worked with Social Security to make it possible to reallocate existing Social Security budgets to avoid the need to introduce a 1% contribution in 2014. This will prevent a further squeeze on Islanders' disposable incomes and at a time when we are supporting the economy through fiscal stimulus.

Budget 2014 goes further though and gives something back to hardworking Islanders who have had to carry on through difficult economic times as we have faced the fallout from the global financial crisis. Our strategic approach to fiscal policy in response to both the move to 0/10 and the need to repair revenues after the global financial crisis has been consistent in focusing on raising revenue through indirect taxation, recognising the risks that other forms of taxation pose to the economy. Having taken these difficult decisions in the past and keeping our finances on a strong and sustainable footing we can afford to give something back. Budget 2014 sets out to do this in a manner consistent with previous fiscal strategies, by cutting the marginal rate of income tax from 27% to 26%.

The reduction in the marginal rate will reduce the tax liability of approximately 84% of the Islands income tax paying population – around 40,000 households. It will put nearly £8m back into Islanders pockets in 2015 after they have experienced a continued squeeze on their incomes in recent years. It will complement the significant capital programme next year and beyond in creating fiscal stimulus that supports employment and growth next year. We can all take reassurance from the Bank of England statements on forward guidance, but Islanders can also take additional confidence from the fact that given our strong financial position we can go further and actually reduce the tax burden for the vast majority of tax payers at a time when we will also be undertaking significant capital investment in the local economy.

Overall Budget 2014 balances the needs for short-term fiscal support to boost employment with the need to underpin economic growth and job creation policies in the medium term. It provides the fiscal stability and certainty that will help growth flourish and at the same time commits to the essential investment the Island needs in areas such as health, social housing and liquid waste. Supporting the economy and investing to improve our competitiveness now will mean we are in the strongest position possible as the global economy continues to improve.

PART F – MAJOR CAPITAL SCHEMES FUNDING OPTIONS

11. Funding Options for the Three Major Schemes

11.1. Introduction

Jersey faces some significant capital investment requirements in the key services areas of health, housing and transport and technical services. Much of Jersey's future capital requirements can be met in the traditional way from current year revenues or from other sources such as capital receipts. However, the following three major schemes demand a re-think of the States' approach to funding major Island infrastructure that has both a long life and long term benefits to the Island.

1. The development of a hospital services and facilities ("the Hospital Project").

2. The need for more and better housing stock ("The Housing Project").

3. The need for an efficient and appropriate Liquid Waste infrastructure for the Island ("the Liquid Waste Project").

This section of the Report summarises the service needs identified by Departments, the likely capital requirements for each project and the potential funding options for consideration and decision.

In brief the funding options that have been explored are:-

1. Borrowing from the external sources ("capital markets").

2. Internal borrowing through investment and subsequent repayment of the States' own resources, for example through an infrastructure investment from the Currency Fund.

3. The use of States existing resources, in particular the proposed limited use of investment returns from the Strategic Reserve Fund.

First of all a reprise of the need for service improvement in these areas. The States has already received very detailed proposals in the Housing Business Case (R015/2013) and the Housing White Paper (P.33/2013) together with the proposition "Health and Social Services: a new way forward" (P.82/2012). The need for the service improvement in these areas has been thoroughly debated by the States but relevant extracts are used in this Report for ease of reference.

The Liquid Waste Project is smaller than those proposed for Health and Housing. Whilst it is a substantial and important project, providing a service critical to our daily lives, it is part of TTS's ordinary business. Even so, the TTS Minister has plans to bring forward a Liquid Waste Strategy for full consideration by States Members and to provide full briefings and tours of the existing plant and equipment to help Members in their deliberations.

12. The need for improvement and replacement of Hospital, Housing and Liquid Waste Facilities

12.1. Hospital Project – The Current Position

Health and Social Services – A New Way Forward

The Health and Social Services Report and Proposition P.82/2012, approved by the States Assembly on the 23rd October 2012, sets out the vision of an integrated care model and a programme of change that will meet the challenges facing the Island's future Health and Social Services.

Central to the development of this vision is the need to have an acute general hospital which is fit for purpose, capable of sustaining the acute care provision requirements for the population and complements the integrated care strategy being developed for Jersey.

Consultation showed that Islanders want Health and Social Services that are:

'Safe' – while many health interventions involve inherent levels of risk, that patients and service users should not be exposed to an undue level of risk.

'Sustainable' – that services should be organised in a way that is not vulnerable to change in the short term.

'Affordable' – that the model of services represents value for money relative to other potential models.

P.82/2012 makes clear that new hospital capacity will be required within 10 years. In fact, bed space is already too constrained and winter pressures could lead to the cancellation of appointments as early as 2014. The Council of Ministers is of the opinion that, given the long lead in time needed to develop new and replacement facilities, construction work should begin without delay in the best interests of protecting the health and safety of Islanders.

The States of Jersey appointed WS Atkins to review the condition and development potential of the existing General Hospital. Their report confirmed the following:

- The total floor area of the combined hospital buildings (circa 38,500m²) is about 60% of that needed for a full new hospital to modern standards (63,600m²).
- A condition assessment carried out in 2008 assessed the majority of the building as being in category C or D – i.e. needing significant investment or replacement.
- Poor configuration and/ or condition meant that some of the existing buildings have limited potential for clinical use or development in a future hospital.
- The layout of the hospital means that there is little opportunity to intensify uses on the current plot and any development would need to be phased.

WS Atkins concluded that a complete redesign and increase in the size of the existing Hospital is required, not only to meet the future acute clinical needs of the growing population of Jersey, but also to address the increase in space standards required to meet current best clinical, spatial and operational practices.

WS Atkins reviewed hospital activity, service development plans and proposals for delivering more health services in the community to establish the scale of future hospital capacity required.

Assuming 2011 Census projections and that proposals within P.82/2012 are successfully implemented, new hospital capacity of circa 300 beds will be required.

Pressures on bed numbers will grow before new hospital capacity is available such that by 2017 up to 50 additional beds will be required to avoid permanent bed crisis.

WS Atkins undertook a Pre-Feasibility Spatial Assessment for the hospital development. Jersey Property Holdings were commissioned to undertake a spatial assessment for new Hospital capacity to inform P.82/2012

- The Planning and Environment Geographical Information System was employed for the subsequent site search.
- A cross-Departmental Officer group reviewed 24 potentially suitable sites and identified a long-list of 11 sites for review by WS Atkins International – a respected hospital master-planning consultant.
- All sites of sufficient footprint (18,000m²) within or adjacent to the Built Up Area were reviewed against set criteria including green and brownfield sites.
- Potential sites suggested by the Minister for Planning and Environment were also reviewed.
- Potential sites were drawn up and evaluated by WS Atkins using cost, benefit and risk criteria. WS Atkins recommend a short-list of 3 sites.

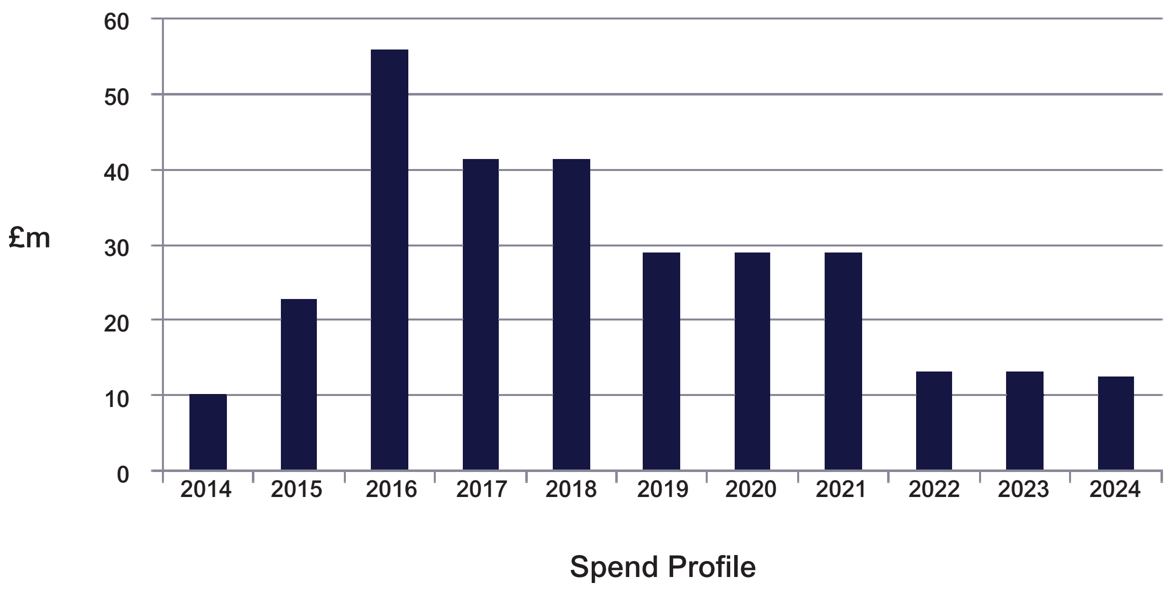
A range of site options were considered and shortlisted to three that have been assessed in more detail. This report does not seek decisions about the final outcome of the process that will determine which of the sites is eventually chosen as the best option nor about the detail of the design and configuration of the buildings.

12.2. Hospital Project Funding Requirements

The same issues and principles need to be addressed when considering funding options, regardless of the final decision on the site and design. This paper is about funding mechanisms. For the purposes of this paper one of the options has been used as the basis for assessing the most appropriate and affordable funding option. This option is summarised in Appendix A at the end of this section. In brief, the costed option is to refurbish and undertake some new building works on the existing site and in addition to develop a substantial new building for the treatment of patients with long term conditions at Overdale. Facilities such as the diabetic clinic, renal dialysis, the pain clinic and day surgery could be included at Overdale in a two site solution that has the potential to maximise the investment made in the existing hospital and provide a long term solution to meet the current and future pressures.

The hospital project is forecast to spend over 10 years from 2014 to 2024. The chart below shows the estimated cost of the hospital project and the estimated spend profile.

FIGURE 22 – ESTIMATED HOSPITAL CAPITAL REQUIREMENTS



	Dec 2014	Dec 2015	Dec 2016	Dec 2017	Dec 2018	Dec 2019	Dec 2020	Dec 2021	Dec 2022	Dec 2023	Dec 2024	Total
£'m	10.2	22.7	55.9	41.4	41.3	28.9	28.9	28.9	13.1	13.1	12.6	297.0

12.3. Housing Project – The current position

There is a requirement to upgrade the social housing stock on the Island to 'Decent Homes Standard' as well as to increase the availability of social housing.

States approval was granted on 16th May 2013 (P.33/2013: The Reform of Social Housing) to enable the Housing Department to become incorporated into a new, not for profit, wholly States owned Housing Company. This will provide the new housing company with powers to borrow in its own right so as to facilitate investment, improved control and management of housing stock.

A key objective for these improvement works is to ensure that the housing stock meets the Decent Homes Standard within ten years.

The structure of the new Housing Association is to be a company limited by guarantee, whose sole guarantor member is the States of Jersey.

Being a company limited by guarantee, the States membership of it is not transferable. The Minister for Treasury and Resources will exercise the powers of the States in their capacity as sole guarantor member and must act in the interest of the States.

Fundamental to the States approving the establishment of the new Housing Company was the production of a Full Business Case. This is set out in R.15/2013 and was presented to the States on 4th March 2013. This makes clear the need for borrowing.

A critical element of the proposed change is that social housing rents are returned to near market fair rents levels.

On 17th July 2013, the States approved the Draft Social Housing (Transfer) (Jersey) Law 201_ (P.63/2013). This is the Law that provides for the States to transfer agreed assets, rights and liabilities to the new company limited by guarantee.

12.4. Housing Project Funding Requirements

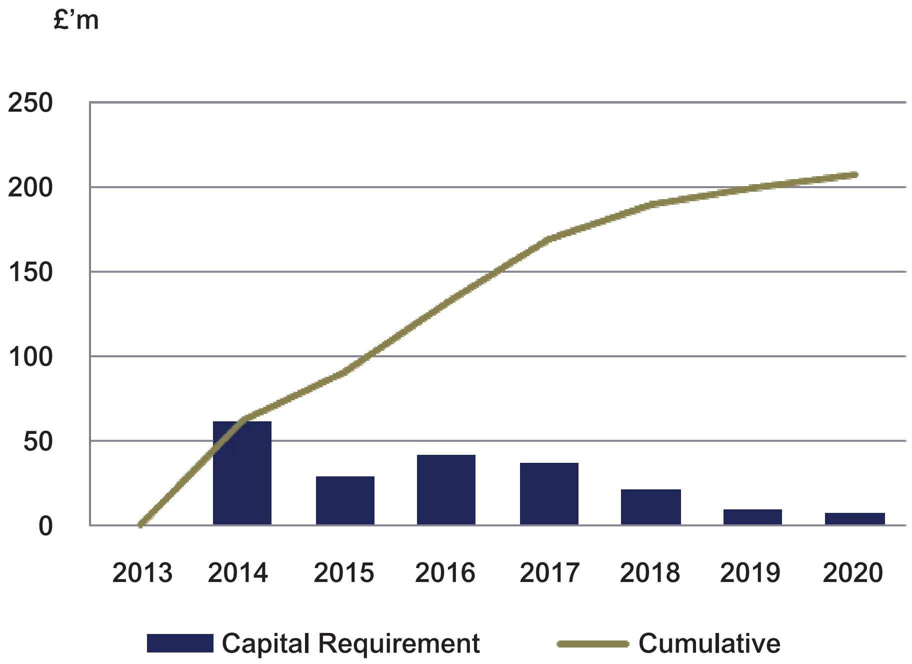
The financial model presented to the States of Jersey as part of the Report and Proposition R15/2013 and P.33/2013 has been used as the basis for estimating the future capital funding needs of the new housing company. The Housing financial model necessarily covered all aspects of service delivery including capital investment, inflation and debt charges. Figure 23 shows the estimated spend profile.

The housing financial model was developed on the basis that the new Company would borrow to meet its spending needs and repay the debt using the rental income associated with the new or refurbished properties.

It is assumed in this report that the interest charge on borrowing for housing purposes should be similar to best current estimates of the coupon rate on a 30 year bond issue. Therefore the interest charge in this report has been estimated at 4.3% (the assumption in the Report and Proposition R.15/2013 and P.33/2013 was a more prudent 5%). This means that if there were any fluctuation in interest rates that Housing have an element of contingency within their financial model. It is assumed that spending on the Housing Project commences in 2013.

A schedule of the housing schemes that could be carried out with this funding is set out in Appendix B at the end of this secton.

FIGURE 23 – ESTIMATED HOUSING TRANSFORMATION CAPITAL REQUIREMENTS



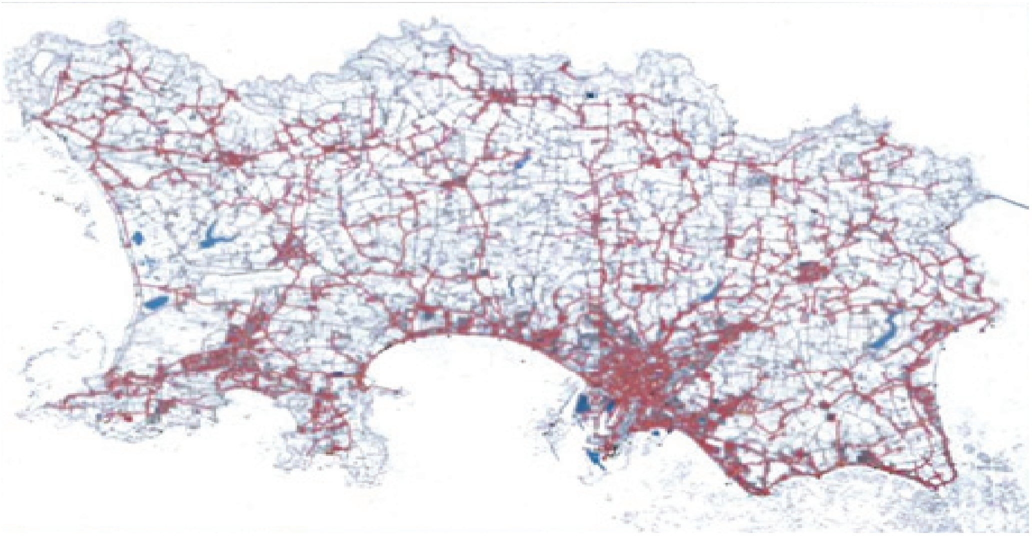
£'m	2013	2014	2015	2016	2017	2018	2019	2020	Total
Housing Transformation	0.3	61.7	28.8	41.5	36.7	20.8	9.7	7.7	207.2

The housing project funding also provides for the repayment to the States of Jersey of £40 million of funding provided to Housing in advance of incorporation so as to facilitate the building of additional homes at a time of economic downturn. This advance funding was provided in the short term, from the Consolidated Fund and will be repaid into the Consolidated Fund and then applied to finance the States' main capital programme as approved in the Medium Term Financial Plan 2013 to 2015.

12.5. Liquid Waste Project – The current position

This investment relates to the Replacement Sewage Treatment Works ('STW') at Bellozane. The safe disposal of Jersey's waste water is vital to keeping the Island safe to live in and its surrounding waters cherished for all aquaculture. This is very much an unseen essential service, a service that may be taken for granted but is critical to public health and safety.

FIGURE 24 – A MAP OF THE ISLANDS SEWERAGE NETWORK



The Transport and Technical Services Department ('TTS') has provided details of the anticipated plan for completion of the works, which is outlined below.

- Q2 2013: Feasibility study completed
- Q4 2013: Tender design complete
- Q3 2014: Planning and Environmental approvals
- Q4 2014: Tender and appoint contractor
- Q4 2014: Demolition and clearance of existing services
- Q2 2015: Clinical Waste Incinerator (CWI) facility relocated
- 2015–2016 : Construction of replacement STW

There is an enormous network of drains (570 kilometres of pipelines) to take the waste water from homes and businesses, a 25,000m³ Cavern storage tank to help cope with storm waters, 116 pumping stations to pump the waste water uphill, an automated monitoring alarm system enabling a quick reaction to problems when they arise, a sewage treatment works and associated plant to separate and treat the liquids and solids and then the drains to send the purified water out to sea.

- Much of the existing network, particularly in St Helier, was built in Victorian times. There is a need for a long-term programme of repair and replacement.
- The network struggles to cope in times of heavy or accumulated rainfall. High rainfall occurs for about a third of the year.

- An inflow and infiltration reduction programme is needed to minimise the amount of water entering the sewage network and thereby reduce costly treatment.

- Whilst flow reduction improves the sewage capacity, it does not affect the *treatment* capacity requirements which are driven by the number of people using the service.

- The cavern fulfils an essential storage role and is in use on average 53 times a year and helps prevent a repeat of the flooding that plagued householders in previous years.

- More storage capacity is needed and this is proposed for the west of the Island. This will reduce the number of spills of diluted waste water from the network.

- The priority is to bring the current network up to the required standard and maintain it in a sustainable manner at this level before expanding the network by adding more properties in areas where it is economically viable.

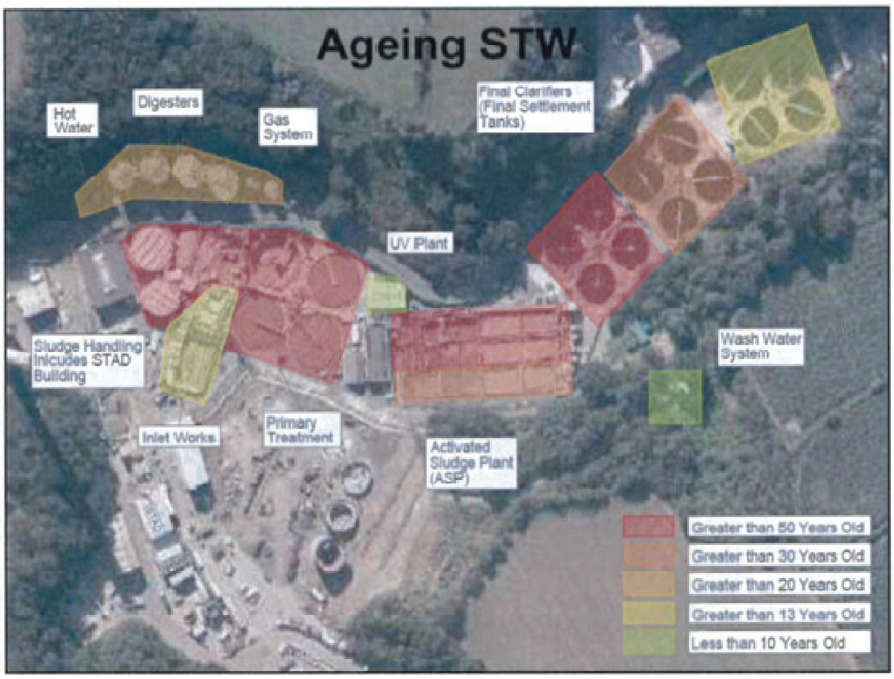
There are three main drivers for change. These are:

- Legal – The current Sewage Treatment Works is breaching consent conditions.

- Operational –the infrastructure is failing leading to high maintenance costs.

- Environmental – Water Framework Directive.

FIGURE 25 – THE AGEING SEWAGE TREATMENT WORKS AT BELLOZANNE



The Bellozanne Sewage Treatment Works is ageing. Almost 50% of the plant is more than 50 years old. High levels of maintenance are required and replacement will provide better value for money over the medium to long term. Current problems include:

- an outdated design;
- difficulty in taking one secondary treatment lane out of service for maintenance without affecting the current overall plant performance;
- poor performance of the high rate aeration system;
- unreliable performance of the secondary treatment process that causes periods of high DO and over aeration;
- poor distribution between final settlement tanks; and,
- limited opportunities for partial upgrades that will meet current and future needs.

FIGURE 26 – THE DECAYING INFRASTRUCTURE FROM THE 1950'S

The Transport and Technical Services Department ('TTS') has provided details of the anticipated plan for completion of the works, which is outlined below.

- Q2 2013: Feasibility study completed.
- Q4 2013: Tender design complete.

- Q3 2014: Planning and Environmental approvals.
- Q4 2014: Tender and appoint contractor.
- Q4 2014: Demolition and clearance of existing services.
- Q2 2015: Clinical Waste Incinerator (CWI) facility relocated.
- 2015-2016 : Construction of replacement STW.

12.6. Liquid Waste Funding Requirements

The Liquid Waste Project draft feasibility study prepared by TTS, estimates the capital costs of the Sewage Treatment Works (STW) Project to be £75m. An analysis of the estimated costs is set out below together with and the estimated profile of spend.

FIGURE 27 – ESTIMATED LIQUID WASTE CAPITAL REQUIREMENTS

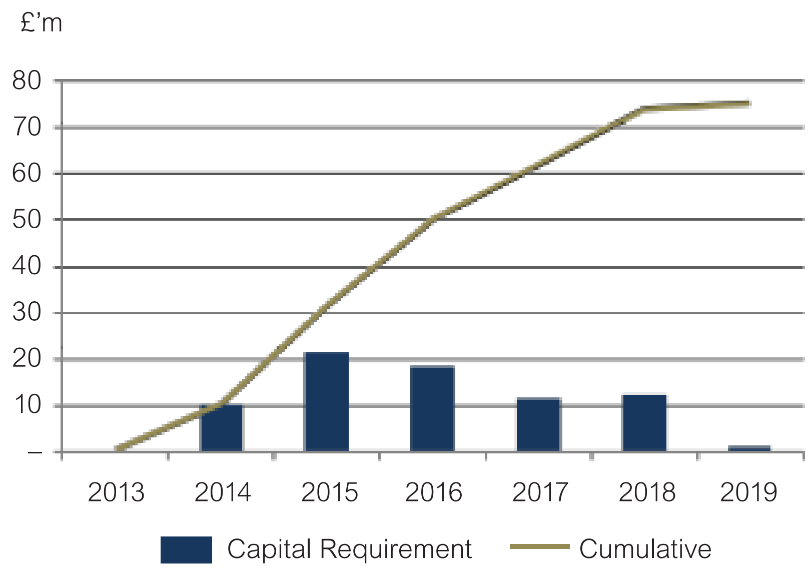


FIGURE 28 – ESTIMATED LIQUID WASTE CAPITAL REQUIREMENTS

£'m	2013	2014	2015	2016	2017	2018	2019	Total
Liquid Waste	0.5	10.1	21.2	18.5	11.4	12.2	1.1	75.0

The technical solutions to solving the challenges of sewage treatment will be fully evaluated and subject to separate detailed reports. The effective operation of the sewage treatment works is a priority for TTS, hence considerable investigative and technical appraisal has been undertaken in the ordinary course of the work of the department. Appendix C at the end of this section provides some further background information on the project in addition TTS extends open invitations to visitors who would like to see the treatment works in operation in order to gain a better understanding of the operational issues at first hand.

This report now focuses on the funding options that are available to meet the costs of investment in the Island's hospital, housing and liquid waste infrastructure.

12.7. Funding options for the three major capital schemes

The Funding Options Available

The previous section of this report has set out in summary the spending needs of the three major capital schemes.

This section of report sets out the funding options available to the States being:

1. borrowing from external sources ("capital markets");

2. internal borrowing through investment of States' own resources for example through an infrastructure investment from the Currency Fund; and

3. the use of States' existing resources.

The Report now deals with each of these funding options in turn.

Borrowing from External Sources: A Brief Overview of the History of Borrowing by The States of Jersey

The States of Jersey has made limited, judicious use of borrowing in the past for the purposes of meeting the cost of major investments in infrastructure that has a long term benefit for the Island. Relevant examples of previous borrowing by the States are set out below.

The Telephone Loans 1970/90 (Jersey) Law 1956

These loans were issued to meet the cost of constructing a new telephone exchange to serve the Central and Millbrook areas and part of the Five Oaks area.

Housing Loans (Jersey) Law 1964

The housing loans were issued "to raise under the guarantee of the General Revenue of the States, loans of a total amount of £2,000,000 for housing purposes. The said loans shall be issued at such times, and in such amounts and subject to such conditions as the Finance Committee may direct, in the form of stock registered in the books of the Treasury of the States, or of bonds payable to bearer, and shall bear interest at such rate as the Finance Committee may determine in relation to the Loan to be issued."

Sewerage Loans 1975/90 (Jersey) Law 1953

These loans were "to meet the cost of construction of public sewers and sewerage disposal works, of acquisition of land or interest in land for the purposes of the disposal of sewerage and generally providing for the sewerage of the Island."

House Construction Loans 1975/95 (Jersey) Law 1960

These loans were issued for housing purposes.

The method used by the States in the past, the issuance of public bonds, to fund Island infrastructure is still a valid option today. However, a range of options have been considered and evaluated and the next section of this Report describes some of the work that has been done.

13. Funding Markets Overview

Summary of the Funding Markets

There are a number of external funding options and markets potentially available to the States of Jersey. These are as follows:

- Rated public bond
- Unrated public bond
- Public retail bond
- Private placement bond
- Project finance
- Bank finance.

The table on the following page summarises the key features of the various external funding options available to the States of Jersey from public bond through to bank debt. The Table shows each of the funding options and characteristics of each. The pros and cons are then summarised. Treasury has considered factors such as: Is the funding denominated in sterling, or will there be currency exchange rate risk? Does the market have sufficient capacity to meet Jersey's needs? Is the term long enough for Jersey's purposes and so on.

Expert advice on external funding options has been taken from Ernst & Young's capital markets team and in the paragraphs that follow there is further detail on each option. Please go straight to the section headed "Summary of the Suitability of Funding Markets" on page 104 if you do not wish to review all of this detail.

FIGURE 29 – SUMMARY OF EXTERNAL FUNDING OPTIONS

	Public Bond (rated)	Public Bond (unrated)	Retail Bond (listed)	US Private Placement	Project Finance	Bank Debt
Currency	GBP, EUR, USD	GBP, EUR, USD	GBP, EUR, USD	USD, GBP	GBP, EUR, USD	GBP, EUR, USD
Liquidity capacity	£200m+ (could go lower with an illiquidity premium)	£200m+ (could go lower with an illiquidity premium)	< £100m	£25-500m	£50m+	£20m+
Maturity	5-50 years	5-50 years	3-10 years	3-30 years	5-25 years	1-7 years
Financial covenants	Typically none	May be required	None	Typically bank style covenants	Required, typically cashflow driven	Yes
Credit ratings	Minimum one required	N/A	Typically required	Private ratings may be required	Not required	Not required
Inflation-linked	Direct is an option	Direct is an option	Direct is an option	Direct is an option	Via swaps	Via swaps
Investor relationships	No	No	No	Yes	Yes	Yes
Pros	• Deep and liquid market • No financial covenants • Historically attractive fixed coupon cost • Long tenors available • Benchmark issue lays ground for future issues	• Reasonably deep market • No financial covenants • Reasonably attractive fixed coupon cost	• Access to alternative investor base • No financial covenants	• No public credit rating required • Historically attractive fixed coupon cost • Flexible maturities available	• Non-recourse bank debt • Suitable for investment capex where there is a construction period • Flexibility in drawdown and repayment profiles	• Simple to arrange • Flexibility in drawdown and repayment profiles
Cons	• Public credit rating and ongoing disclosure requirements • Minimum deal size of £200m • Early redemption costs	• Price premium compared to rated public bonds • Minimum deal size of £200m • Early redemption costs	• Bespoke disclosure and documentation requirements • Less capacity than public market	• Financial covenants required • Early redemption costs • Typically more costly than public markets • Long dated swaps would be required	• Security required • Can be complex in structuring • Lengthy arrangement process	• Shorter tenors than other markets • Refinancing risk
Pricing	10yr: Gilts + c. 65bps 30yr: Gilts + c. 80bps	10yr: Gilts + c.90 bps 30yr: Gilts + c.105 bps	10yr: c. 4.5% 30yr not likely available	10yr: Gilts + c.115 bps 30yr :Gilts + c. 130 bps	25yr: LIBOR + c.275 bps	10yr not likely available

Public Bond Markets

A decision for the States to take external borrowing would mark a significant departure from previous practise unless certain conditions are satisfied. First the States does not borrow to meet current year expenditure. The three major projects are all investments that will serve Islanders for at least two generations. Secondly the States must be able to maintain its strong and stable balance sheet and repay the debt, both principal and interest. If the borrowing is taken for housing purposes then this can be achieved with rental income used to repay the debt. Financial assets (cash) on the Balance Sheet is replaced by physical assets (housing) in a company wholly owned by the States.

The next part of the Report provides detailed information on funding markets – some readers may prefer to move straight to section 3.2 which deals with their suitability for Jersey.

Market backdrop

Public bonds are priced with reference to benchmark 'risk free' rates (for example UK Gilts in the Sterling market and German Bunds in the European markets). As highlighted in the graph below, benchmark rates are currently near historic lows which has led to opportunities for issuers to raise long term fixed rate debt at record low coupons (interest rates).

The market for bonds will be dependent on a clear communication of the credit proposition by the States, a well structured marketing process and an appropriately priced and sized offering.

Despite the economic downturn, the public bond market continues to show interest in lending to organisations like the States of Jersey with a strong credit history. This is evidenced by the number of successful issuances over the last year.

The public bond market offers the opportunity to raise significant sums with a "bullet" payment to repay the principle at the end of the period.

The chart below shows that the Sterling public bond market has continued to offer an available source of finance for sovereign countries. 2012 has seen a sharp increase in the number of deals of a size comparable with the possible funding requirement for the States of Jersey.

FIGURE 30 – GOVERNMENT BENCHMARK BOND YIELDS

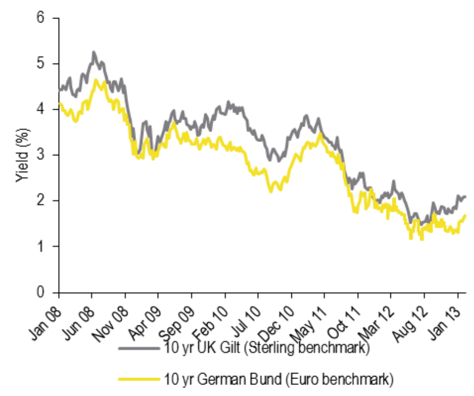
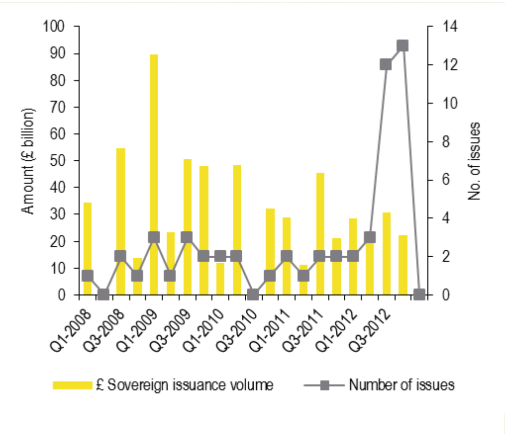


FIGURE 31 – SOVEREIGN ISSUANCE IN THE £ BOND MARKET



Sterling bond market

The Sterling bond market offers a route for the States of Jersey to raise long term debt finance.

The Sterling market offers adequate depth to provide a first time issuer like Jersey with a level of financing that would meet our requirements. It is market standard that an issuance is a minimum of c.£200m to create adequate liquidity in the security.

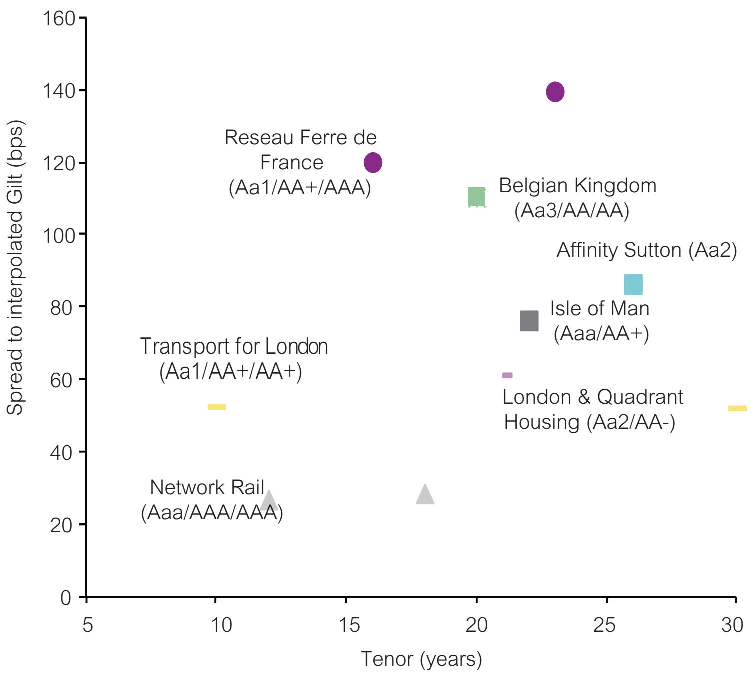
The pricing of recently issued bonds that those issuers with a close link to the UK Government (e.g Network Rail, Isle of Man) achieve the lowest cost of funds, followed by Government related entities (e.g. Housing Associations). Pricing varies from a spread of c.55 – 77 bps for a 10 year bond increasing to potentially over 150bps for a 25 year AA-rated bond due to the credit quality of the borrower. (A "spread" just means the amount of interest paid above a benchmark rate, typically base rate. "Pricing" simply means the interest rate that is paid). It must be noted that pricing (the interest rate paid) varies over time due to movements in the underlying benchmark (typically base rate) and spreads (the premium paid above base rate – the worse the credit rating of the borrower, the higher the premium paid because of the risk of default).

Of the comparables identified below the States of Jersey is most closely comparable to Transport for London due to both these entities being domestic issuers and having a link to the UK Government. These historical deals are shown for reference purposes only. They give a helpful indication of the extent to which interest rates vary with the period over which the funds are borrowed. This loan period is referred to as the "tenor".

FIGURE 32 – PRIMARY STERLING MARKET HIGH INVESTMENT GRADE ISSUANCE

Date	Issuer	Rating (M, S&P, F)	Amount (£m)	Tenor (years)	Coupon	Spread (G+bps)	Mandated Lead Arranger
Jan -13	Network Rail	Aaa, AAA, AAA	750	4	1.000%	28	Deutsche Bank, HSBC, RBS
No v-12	Nestle	Aa2, AA, AA+	400	10	2.250%	65	Barclays, Goldman Sachs, HSBC, RBS
No v-12	Transport for London	Aa1 AA+, AA+	300	5	1.250%	55	Barclays, HSBC, Morgan Stanley
Oct-12	Deutsche Bahn	Aa1, AA, AA	300	5	1.375%	41	Barclays, Credit Suisse, Mitsubishi
Oct-12	University of Cambridge	Aaa NR, NR	350	40	4.750%	65	HSBC, RBS, Morgan Stanley
Aug -12	Transport for London	Aa1 AA+, AA+	500	10	2.250%	77	Deutsche Bank, Goldman Sachs, HSBC
Aug -12	Libra Treasury	Aa3, NR, NR	250	26	5.125%	169	Barclays, Lloyds
Jul-12	Transport for London	Aa1, AA+, AA+	500	30	3.875%	65	Deutsche Bank, Goldman Sachs, HSBC

FIGURE 33 – SECONDARY STERLING MARKET COMPARABLES



Euro bond market

The Euro bond market is open and active and can offer lower coupons than the Sterling bond market for certain issuers. This is due to the benchmark rate (i.e. Bund rate) currently being lower than the benchmark rate (i.e. Gilt rate) in the Sterling bond market. However, tenors achievable are typically shorter than the Sterling bond market with issuance over 10 years being rare.

As with the Sterling market, domestic issuances from European entities achieve the best pricing. Therefore, the States of Jersey may have to offer Euro bond investors a small premium compared to a European based issuer.

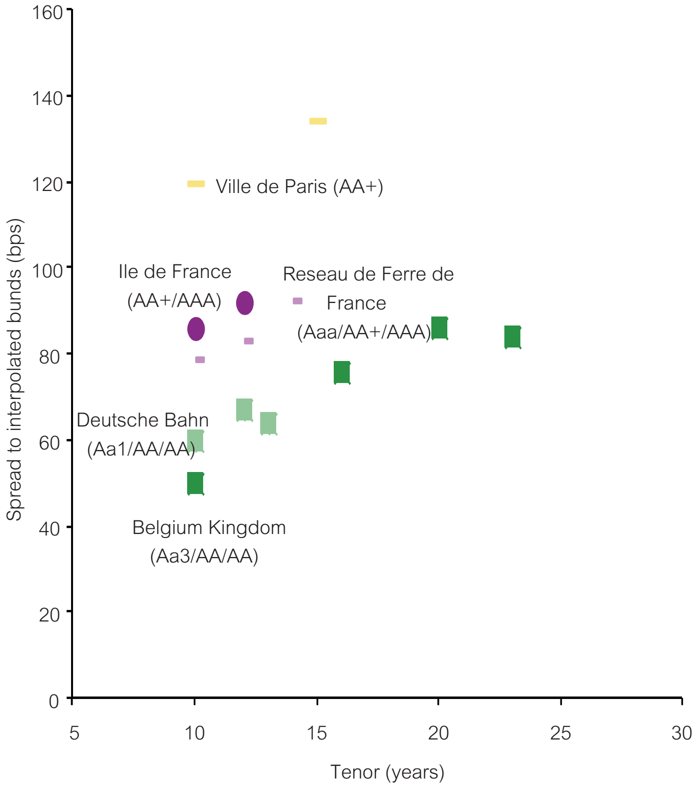
The Euro bond market's suitability for the States of Jersey is limited as the States of Jersey has very little revenue that is denominated in Euros (i.e. only a few million pounds per year income for the airport). This means that although it might have a lower coupon, there is significant currency risk on the repayment of principal.

This risk could theoretically be hedged, but the cross-currency swap will add to the risk and cost of the bond issue.

FIGURE 34 – PRIMARY EURO MARKET STATE-LINKED ISSUANCE

Date	Issuer	Rating (M, S&P, F)	Amount (€m)	Tenor (years)	Coupon	Spread (B+bps)	Mandated Lead Arranger
Jan-13	Sweden	Aaa, AAA, AAA	4,000	5	0.880%	23	Danske, Goldman Sachs, JP Morgan, RBS
Jan-13	Kingdom of Belgium	Aa3, AA, AA	4,000	10	2,250%	62	Barclays
Oct-12	State of Nordrhein-Westfalen	Aa1, AA-, NR	300	10.5	2.000%	50	Barclays, Landesbank Baden-Württemberg, Commerzbank
Sep-12	Stockholm	Aaa, AA+, NR	500	10	2.125%	62	-
Sep-12	State of Nordrhein-Westfalen	Aa1, AA-, NR	750	10	1.875%	46	DZB Bank, HSBC, Natixis Unicredit
Aug-12	State of Berlin	Aa1, NR, AAA	250	8	1.500%	49	Landesbank Baden-Württemberg, Unicredit, WGZ Bank
Aug-12	State of Brandenburg	Aa1, NR, NR	150	8	1.500%	53	WGZ Bank

FIGURE 35 – SECONDARY EURO MARKET COMPARABLES



Considerations as to the Size of The Bond Issuance

Typical investors are large sophisticated institutions. The liquidity of a transaction is of critical importance to investors and a minimum size of £200m–£250m is typical because of concerns over liquidity, index eligibility and the size of the ultimate holding.

FIGURE 36 – CONSIDERATIONS AS TO THE SIZE OF BOND ISSUANCE

Issue Size	£125m and less	£175m	£200m	£250m
Comment	Some investors may not participate given sub £200m ('benchmark') size and others are likely to demand an illiquidity premium	Preferable to a £150m issue, however, similar concerns over liquidity apply	Most sterling investors would view a transaction of this size to be of interest, but remains ineligible for the iBoxx index	Optimal size, which is eligible for all indices and will be viewed as relatively liquid
Pricing impact	+ c.15-25bps	+ c.5-10bps	+ c.0-5bps	None

FIGURE 37 – BOND INDEXES – FOR TRADING PURPOSES

Index provider	Relevance	Threshold
markit	High	£250m
Bank of America Merrill Lynch	High	£100m
BARCLAYS CAPITAL	Low	£200m

Bonds on the public market can be openly traded after issuance and holders of the securities can change many times. Investors will therefore ask for liquidity and would want bonds to be included in one or more indices. Bonds that are liquid and regularly traded are sought after and tend to attract tighter pricing (that is, lower interest rates). This is because it makes it is easier for holders to sell these instruments in the secondary market.

The inclusion of the bond on one or more indices will mean that the price movement of the bond, once issued, will be open and transparent.

The indices comprise a vast universe of bonds that contribute to their price. For example, the Markit iBoxx Sterling Benchmark Index had more than 1,000 constituents totalling £1.5tn (at the end of 2011). Therefore an issuance by the States of Jersey would not move the index, the bonds would be more easily tradeable and therefore more liquid and attractive to investors.

Rating considerations

In order to issue in the public bond markets it is standard market practice that an issuer will obtain at least one public rating from either Moody's, S&P or Fitch. It is more common that an issuer will have two ratings. Public credit ratings provide investors with a level of transparency and assurance to allow them to fully understand the credit profile of the bonds being offered. Unrated issues tend to be reserved for well known large entities with a well understood credit profile. Unrated issuance from Government related entities is extremely rare. Further information on credit ratings and the process of getting and managing a credit rating is set out in Appendix D at the end of this section.

Public Bond Markets Considerations

Retail bonds offer an alternative source of funding

Whilst public bonds are traditionally bought by institutional investors, an alternative option is to target retail investors (private savers). Listed retail bonds are sold through a network of brokers and are tradeable on the London Stock Exchange Order Books for Retail Bonds ('ORB') platform. Since the ORB platform was launched in 2010, it has raised £2.8bn for a number of corporates.

The retail bond market allows issuers to offer their stakeholders (customers, employees, residents) the opportunity to be part of their development through investment in the issuer, whilst in many cases providing savers with an attractive yield on their investment when compared to traditional savings products.

In 2011 the Belgian government launched a €200m bond issue targeted at retail investors, this was increased due to strong demand and closed at €5.7bn. Investors were offered a 4% coupon for the 5-year deal.

A retail bond could potentially provide an opportunity to attract local Jersey non-institutional investors. However, as seen in the table below, the Sterling retail bond market cannot provide either the tenor or the quantum required by the States of Jersey to meet its funding requirements. It would also be likely to price significantly higher than an institutional bond of equivalent tenor and size and therefore would be a more expensive route than borrowing from institutions.

FIGURE 38 – NEW ISSUES ON THE ORB LISTED BOND MARKET

Date	Issuer	Amount (£m)	Tenor (years)	Coupon
Feb-13	En Quest	145	10	5.500%
Dec-12	Alpha Plus	48.5	7	5.750%
Dec-12	UNITE Group	90	8	6.125%
Dec-12	Tullet Prebon	80	7	5.250%
Oct-12	London Stock Exchange	300	9	4.750%
Oct-12	St. Modwen Properties	80	7	6.250%
Oct-12	Workspace	58	7	6.000%
Sep -12	Intermediate Capital Group	80	8	6.250%
Sep -12	CLS Holdings	65	7	5.500%
Jul-12	ICAP	125	6	5.500%
Jul-12	Primary Health Properties	75	7	5.375%
Jul-12	Severn Trent	75	10	RPI lin ked
May-12	Tesco Personal Finance	200	8	5.000%
May-12	HSBC	196	3	2.875%

Private Placement Bond Market

The Private Placement bond market has seen volumes surge and pricing fall.

The Private Placement market has been robust, has remained open and shown continuing investor appetite throughout the period since 2008 despite wider market volatility. This is demonstrated by the issuance volumes in the chart below, with the two most active months of the last three years occurring in 2012.

A Private Placement bond is typically sold directly to one or more sophisticated institutional buyers, with the major investors in the market being the US and UK insurance companies. UK insurance companies, like M&G and Aviva UK, are very active in the Sterling private bond market. The typical size range for a private placement bond is in the region of £25m to £500m.

In contrast to the public market, the bonds cannot be exchange-traded after issue. As such, private placement issues generally tend to attract an illiquidity premium and as such, have higher spreads and price slightly higher than in the public bond market.

In the private placement market there will typically be a smaller number of investors and they will have a direct relationship with the issuer, allowing for a more bespoke negotiation of structure and terms. Furthermore, the issuance could also be kept private and not disclosed to the public market.

Due to the lack of rating requirements and not being listed on any exchange, a much lower level of ongoing disclosure is required than in the public bond market, however the pricing tends to be more expensive than a public bond. Whilst a public credit rating is not essential, the bonds would receive a credit designation from the National Association of Insurance Commissioners ('NAIC', the US insurance regulator) if any US investors took part in the deal. There is also the option to seek designation from the NAIC before the bonds are issued.

FIGURE 39 – NAIC-1 NEW ISSUE USPP SPREADS TO US TREASURIES

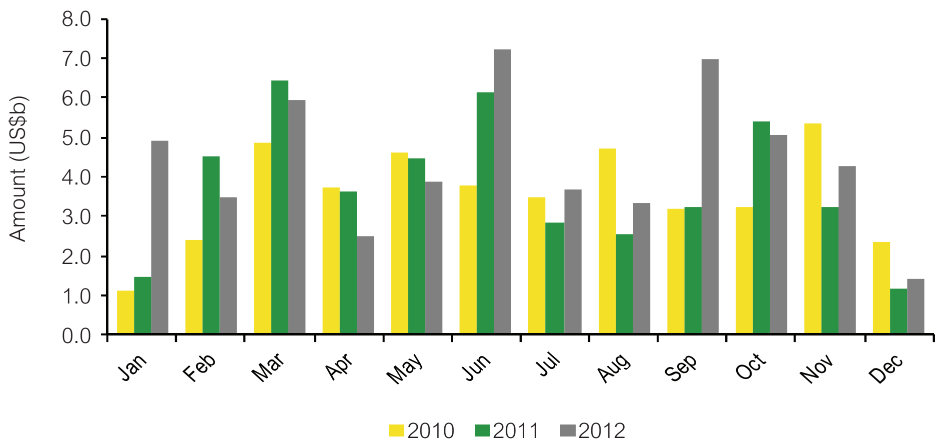
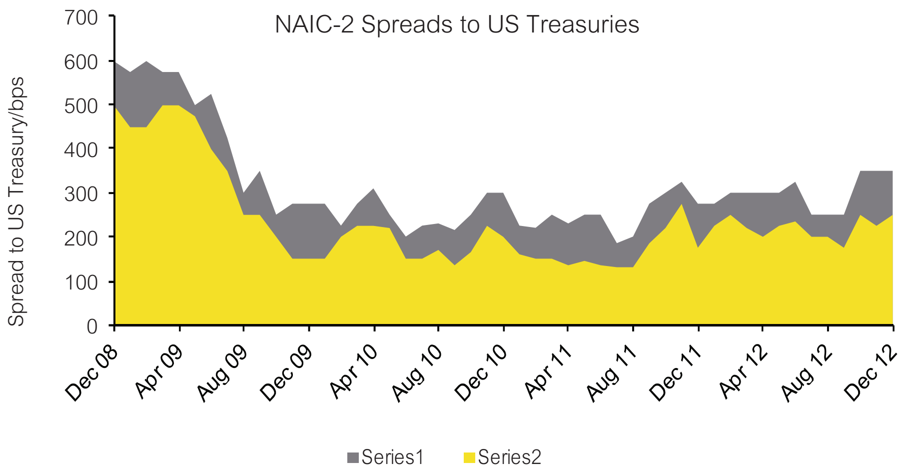


FIGURE 40 – U.S. PRIVATE PLACEMENT ISSUANCE VOLUMES



Issuance in the U.S. Private Placement Market is limited and is infrequent from sovereign entities.

Sovereigns and sub sovereigns, including British overseas territories, have not ventured into the private placement market very frequently. The most recent was in 2009.

Sovereign linked or sovereign backed corporates have accessed the private placement market in the recent past including JT Group Limited in the Summer of 2012. JT Group Limited issued £51m of notes in two tranches, £31m of 3.86% 2019 notes and £20m of 4.48% 2022 notes.

Pricing in the private placement market is likely to be slightly wider (more expensive) than the public bond market to compensate investors for the lack of liquidity. From an issuer's perspective however, the transaction costs involved with a private placement are lower than those of a public bond deal.

Spreads in the private placement market have tightened (become less expensive) over time with spreads for a strong AA rated entity currently ranging from 150–200bps.

FIGURE 41 – PRIVATE PLACEMENT MARKET COMPARABLES

Date	Issuer	Rating (M, S&P)	Amount (US$m)	Tenor (years)	Coupon	Spread (T+bps)
Nov-09	Government of Bahamas	A3, BBB	300	20	-	T+275
May-09	Government of Bermuda	Aa2, AA	160	5 7 10	6.550% 6.980% 7.380%	T+450 T+425 T+425
Sep-08	Washington State Investment Board	NR, NR	625	3	-	T+225
Dec-07	Commonwealth of Pennsylvania	NR, NR	27	24	-	T+160
Nov-07	Government of Bermuda	Aa2, AA	140	15	-	T+150

Structure considerations

The majority of investors are US based and are providers of US Dollar denominated funds. Some will offer a cross currency swap. Such an approach would, however, require "swap breakage indemnification". In the event of early repayment by the borrower, investors use the indemnification to protect themselves from losses arising on the unwinding of interest rate and cross currency swaps initially taken out to provide Sterling funding.

Medium to small US based investors currently have limited appetite for undertaking cross-currency swaps, however large investors are very capable of undertaking this type of structure, including London based US investors. Additionally, there have been a few instances where some investors are willing to forgo swap breakage indemnification in order to participate in issues they feel to be particularly attractive. This is achieved through the use of a counterparty, thus eliminating the need for protection on unwind.

From Jersey's point of view a sterling denominated bond presents both less risk and lower cost.

Project Finance

Project finance could potentially be raised against the specific assets being financed

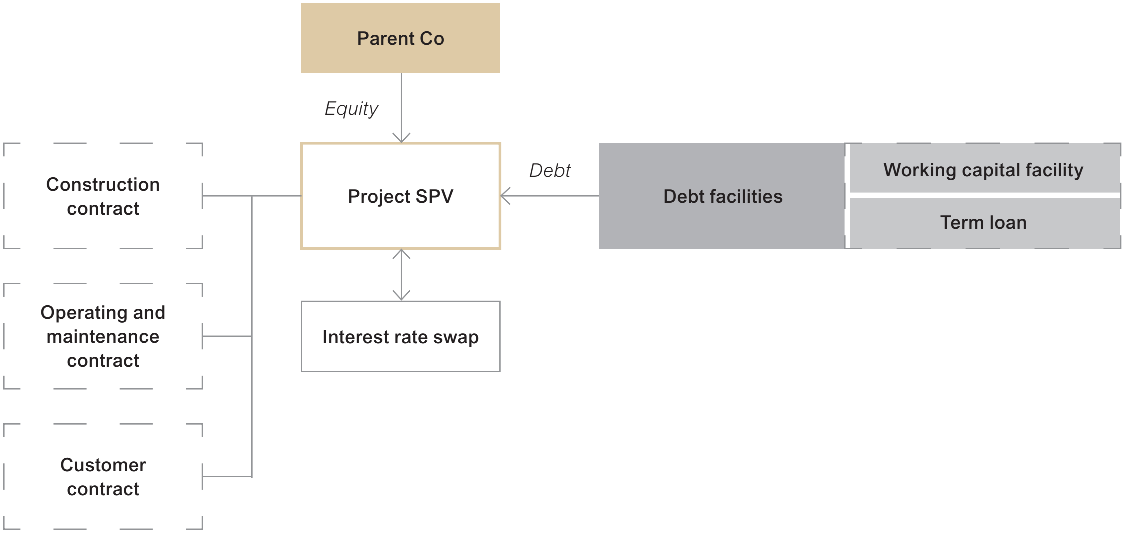
A secured project finance facility is also a potential source of finance for the capital projects where funding profile and repayment is matched to the specific cash needs and flows of a specific project.

A traditional project finance structure is outlined below and involves a 'Project Company' special purpose vehicle ('SPV') being set up as the borrowing entity, as well as the contracting entity, for construction contracts and customer contracts. The terms available to the SPV are based on the profile and cash flow of the project and not necessarily the underlying corporate credit quality.

If the States of Jersey were to pursue a project finance structure, a guarantee from the States of Jersey to the SPV would help significantly lower the cost of debt.

Project finance debt can be provided by banks (as has traditionally been the case) or by an institutional lender. Aviva, for example, has recently provided debt in a number of public sector infrastructure deals.

FIGURE 42 – A TYPICAL SPECIAL PURPOSE VEHICLE STRUCTURE FOR FINANCING PROJECTS



Project finance facilities allow for more bespoke matching of project cash flow profiles to drawing of finance

A disadvantage of financing a project with a bond solution is that the typical phased capital requirement of a project does not align with the immediate drawn nature of a bond financing. A negative cost of carry may therefore be incurred if finance is drawn down and funds remain in a bank account, earning a lower rate of interest than the cost of borrowing.

A project finance structure would allow a gradual draw down of funds and therefore interest is only incurred as and when the capital requirement arises. The portion of the facility that remains undrawn would be subject to a non-utilisation or commitment fee.

FIGURE 43 – PROJECT FINANCE MARKET COMPARABLES

Date	Project	Debt raised (£m)	Tenor (Years)	Margin (bps)	Mandated Lead Arrangers
Oct-12	Avon & Somerset Police	76	26	-	Aviva
Aug-12	Sheffield Highways	212	-	-	Lloyds, NordLB, KfW, Sumitomo Mitsui
Aug-12	Hounslow Highways	110	24.5	250	Bank of Tokyo Mitsubishi, DZ Bank, KfW, Sumitomo Mitsui
Aug-12	University of Essex Student Housing	50	35	-	Aviva
May-12	Essex Waste	165	26	350-400	Sumitomo Mitsui, BayernLB, NordLB
May-12	Lambeth Myatts Field North Housing	72	24	-	NordLB, Co-operative, NAB
Apr-12	Barnsley Doncaster and RotherhamResidual Waste	90	23	250-300	Lloyds, Sumitomo Mitsui
Feb-12	Nottingham Trent University Accommodation	45	5	-	RBS
Feb-12	University of Reading Accommodation	186	-	-	Aviva
Feb-12	Norfolk Waste	90	25	305-340	RBS, Lloyds, Sumitomo Mitsui
Dec-11	Kirklees Social Housing	79	22	235-255	NordLB, Co-Operative, Nationwide
Nov-11	Salford and Wigan Schools	75	27	275	NordLB

Impending regulatory reform (in the form of Basel III) combined with volatile wholesale funding markets are affecting bank appetite for long term Project Financing. As a result, margins are creeping up with c.25 year funding costing over 350 bps in some cases.

From The States point of view this is not, therefore, the most efficient borrowing option.

Bank Finance

Traditional bank finance is used by sovereign entities, but commonly by those with a weaker credit profile than the States of Jersey.

High investment grade sovereign entities are infrequent borrowers in the bank market. Recent loan funding in Europe has stemmed from nations at the centre of the Eurozone crisis, namely Spain and Portugal. Developing economies that do not have ready access to the capital markets have also turned to the bank market for support.

FIGURE 44 – BANK LOAN MARKET COMPARABLES – SOVEREIGNS

Date	Borrower	Rating (M, S&P, Fitch)	Currency	Form	Debt raised (m)	Tenor (Years)	Margin (bps)1	Mandated Lead Arrangers
Nov-12	Republic of Macedonia	NR, BB, BB+	EUR	Term	250	7	N/D	-
Oct-12	Diputacion de Vizcaya	Baa2, BBB+, AA	EUR	Term	72	7	N/D	BBVA, Kutxabank
Oct-12	Republic of Ghana	NR, B, B+	USD	Term	162.6	12	N/D	Citi, JP Morgan
Sep-12	Republic of Angola	Ba3, BB-, BB-	JPY	Term	30,800	8	N/D	Japan Bank for International Cooperation, Bank of Tokyo Mitsubishi
Sep-12	Republic of Angola	Ba3, BB-, BB-	JPY	Term	30,200	8	N/D	Japan Bank for International Cooperation, Bank of Tokyo Mitsubishi
Jun-12	Province of Quebec	Aa2, A+, AA-	CAD	RCF	3,500	3	N/D	CIBC, RBC, TD
May-12	Republic of Kenya	B1, B+, B+	USD	Term	600	2	475	Standard Chartered, Citi, HSBC, PTA Bank
Feb-12	Dubai	NR, NR, NR	USD	Islamic	137	6	N/D	Deutsche Bank, Citi, HSBC
Feb-12	Dubai	NR, NR, NR	USD	Islamic	137	6	N/D	Deutsche Bank, Citi, HSBC
Feb-12	Dubai	NR, NR, NR	USD	ECA	401	13	N/D	Deutsche Bank, Citi, HSBC
Nov-11	Diputacion de Vizcaya	Baa2, BBB+, AA	EUR	Term	168	8	340	Banco Guipuzcuano, BBVA, Bilboa Bizkaia Kutxa, Caixabank, Caja Laboral, Ipar Kutxa

Due to the Eurozone debt crisis, banks have experienced an increase in their own cost of finance, driving loan margins upwards. Margin increases, however, to an extent been mirrored by falls in LIBOR and EURIBOR rates.

However, requirements on tenor are far more restrictive with the tenor available in the bank market being much shorter than the capital markets. The sovereigns that have accepted shorter term bank financing tend to be driven by an inability to access the capital markets (typically due to lack of investor appetite due to concerns over credit strength).

The requirement to hold more Tier 1 capital has resulted in capital constraint for banks, reducing available capital and lending capabilities.

Jersey's financial position and strong balance sheet means that the Island has more cost effective means of borrowing than bank debt for funding these three major capital projects

Summary of the Suitability of Funding Markets

A number of factors have been considered when assessing the suitability of funding markets for the States of Jersey

The following factors were considered for each funding market.

FIGURE 45 – A SUMMARY OF THE SUITABILITY FOR JERSEY OF DIFFERENT FUNDING MARKETS

Considerations	Relevance to the States of Jersey	Conclusion
Currency	As the States of Jersey generates a large portion of its revenue through taxation, which is denominated in Sterling, raising debt in Sterling avoids costs associated with cross-currency swap agreements. Therefore, raising debt in Sterling is deemed more suitable for the States in Jersey.	Direct Sterling most suitable
Financing requirement	The capital requirements of the three major projects is significant. (Please note that borrowing is only one of the funding options).	Market depth of up to £250m may be required.
Tenor	A long dated issuance is appropriate to fund the long term nature of the projects being financed.	10–40 years.
Coupon type	A fixed coupon (interest rate) provides certainty over interest payments and avoid costs associated with swap agreements. Therefore, a fixed coupon is deemed more suitable for the States of Jersey as it protects against fluctuations in interest rates.	Fixed rate.
Repayment	The projects being funded are not expected to generate significant cash for principle repayment. However, the States is very unlikely to want to adopt the approach that many governments take and roll over debt from one loan to the next. The States will plan for the repayment of debt by building a fund so as to repay the debt at the end of the period.	Bullet structure with a separate fund built up over time to repay the debt.

The markets reviewed are summarised below for their suitability against the States of Jersey's requirements

Public bond market

The public bond market provides the opportunity to raise funds for tenors ranging from as short as 3 years to as long as 50 years.

The appetite for bonds and the success of an issuance in the public market is dependent on a clear communication of the credit proposition and a coherent rationale for the proposed issuance.

Therefore, it would be important that the States of Jersey clearly communicates its credit profile to the market. As a new issuer accessing the public bond market, a public credit rating would help the States of Jersey present its credit profile and position itself amongst its peers. Furthermore, it would also facilitate the achievement of a more competitive coupon rate (interest rate) than an unrated bond.

The Sterling public bond market provides sufficient capacity to raise the amount required by the States of Jersey to meet its funding needs, in the currency required. It also offers the States of Jersey the opportunity to access long term bullet maturity, fixed rate finance at historically low levels.

The Treasury view, informed by advice from Ernst & Young, is that the rated public bond market is the suitable option to meet the States of Jersey's requirements for borrowing, provided that the States is minded to use borrowing as a means of funding infrastructure investment. The project most suited to being funded from borrowing is Housing because the rental income stream can be used to repay debt.

Retail bond market

The average deal size achieved in the retail bond market since the beginning of 2012 is c.£110m, which is below the debt financing requirement of the States of Jersey.

Furthermore, the maximum tenor achievable in the retail bond market is c.10 years. Individual savers (the buyers of retail bonds) have different priorities to institutional investors and are less likely to want to lock up funds for the long term.

A retail bond, therefore, is not likely to be a suitable option to provide the States of Jersey with the capital and tenor required.

Private placement market

The private placement market provides the States of Jersey with the opportunity to raise the quantum required for durations of up to 30 years at a cost of Gilts+150–200bps.

Although the private placement market does not have any public rating requirements and has less onerous disclosure requirements than the public bond market, private placements price slightly wider (are more expensive) than public bonds. As a result of this, sovereign entities tend to access the public bond market rather than the private bond market where tighter (cheaper) pricing can be achieved, due the depth of secondary market liquidity (the extent to which bonds can easily be bought and sold).

Furthermore, raising the required funds in Sterling from US based investors may also prove challenging due to the likely requirement for cross currency swaps.

Therefore, due to the higher cost of finance and the potential challenges associated with raising the required funds in Sterling (depending on the amount sought), the private placement market is not likely to be the most suitable option for the States of Jersey's financing requirements.

Project finance

The amount of capital banks are required to raise to comply with Basel III will depend on the profile of their lending activities, with credit risk, liquidity, and tenor all playing a part in determining the capital weighting of each exposure. Project finance lending is expected to attract large capital weightings due to the long tenor, relative illiquidity and bespoke nature of each financing.

As a result, bank appetite for project finance debt is reducing, with prices rising, and tenors decreasing.

Whilst tenors of up to 25 years may be achievable, margins on this tenor may be higher than other funding markets.

Project finance requires the underlying assets to have strong cash flows associated with them. This is not the case for the Hospital Project or the Housing Project in earlier years.

Therefore, project finance would be more expensive than bond finance and would also prove challenging to access in the current market. It is not likely to be a suitable form of financing for the States of Jersey.

Bank market

Bank market finance can be simple to arrange, provides flexible drawdown profiles and is also less onerous as there are no credit rating requirements. In addition, the bank market also facilitates raising the required amount of funds in Sterling.

However, despite the benefits of this source of funding, the tenor available in the bank market is much shorter than that available in the capital markets. The shorter-term nature of this funding source would not meet the States of Jersey's requirement for long term financing.

Furthermore, interest on bank market funding is generally floating with reference to a relevant interbank rate. As such, there is likely to be uncertainty associated with debt servicing costs. This uncertainty could be hedged through swap agreements. However, there would be costs associated with entering into swap agreements.

The bank market could be a suitable short-term financing option for the States of Jersey, but is unlikely to meet its medium and long term requirements.

Summary of Funding Market Suitability

FIGURE 46 – ASSESSMENT OF FUNDING MARKET SUITABILITY

	Public Bond (rated)	Public Bond (unrated)	Retail Bond (listed)	US Private Placement	Project Finance	Bank debt
Currency - GBP	✓	✓	✓	✘	✓	✓
Liquidity capacity	✓	✓	✘	✓	✓	✓
Tenor - 10 to 40 yrs	✓	✓	✘	✓	✓	✘
Benefit from a credit rating	✓	✘	✓	✓	✘	✘
Direct inflation-linked	✓	✓	✓	✓	✘	✘
Coupon type – fixed	✓	✓	✓	✓	✘	✘
Maturity type – bullet	✓	✓	✓	✓	✘	✘
Transaction costs (upfront fees)	✓ Lower than the bank market	✓ Lower than the bank market	✓ Lower than the bank market	✓ Lower than the bank market and the public	✘ Higher than the public bond market	✘ Higher than the public bond market
Transaction costs (ongoing costs)	✘ High transaction costs	✘ High transaction costs	✘ High transaction costs	✓ Lower than the public bond market	✓ Lower than the public bond market	✓ Lower than the public bond market
Disclosure requirements	✘ Onerous disclosure requirements	✘ Onerous disclosure requirements	✘ Onerous disclosure requirements	✓ Less than the public bond market	✓ Less than the public bond market	✓ Less than the public bond market
Pricing	✓ Lowest pricing achievable	✘ Wider than the rated public bond market	✘ Wider than the institutional bond market	✘ Higher than the public bond market	✘ Higher than the private bond market	✘ Higher than the rated public bond market
Suitability for Jersey	✓ Can provide tenor and quantum of funds sought	✘ Can provide tenor but pricing likely to be higher than a rated public bond	✘ Unlikely to offer capacity and tenor required	✘ Pricing likely to be higher than public market	✘ Likely to be costly, complex and time consuming	✘ Unlikely to offer tenor required

14. Funding Strategy – Servicing the Debt

Indicative Interest Costs

Should a bond be issued, the States of Jersey would need to service its debt annually.

The pricing below is undertaken based on Gilt rates and spreads as at 14 February 2013.

Assuming that the States of Jersey receives a 'AA+/Aa1' credit rating, indicative assumptions on pricing are set out in the table below.

FIGURE 47 – THE PRICING OF UK GILTS FOR DIFFERENT TENORS (FEB 2013)

	10 year	15 year	20 year	25 year	30 year	40 year
UK Gilt rate (%)	2.10%	2.65%	3.00%	3.25%	3.34%	3.47%
Credit spread for a AA+ rated entity	65–100 bps	65–105 bps	70–110 bps	75–120 bps	80–125 bps	80–125 bps
Total coupon (%)	2.7%–3.1%	3.3%–3.7%	3.7%–4.1%	4.0%–4.4%	4.1%–4.6%	4.3%–4.7%

It must be noted that the pricing in the above table will move over time as Gilt rates and spreads move.

Should the States of Jersey choose to issue an unrated bond, the credit spreads would increase (become more expensive) from those shown in the table above, the pricing differential varies at different points in the market but may be in the range of 20–30bps.

FIGURE 48 – INDICATIVE INTEREST COSTS FOR LONG TERM BORROWING

	10 year	15 year	20 year	25 year	30 year	40 year
Assumed debt (£ million)	£200 million	£200 million	£200 million	£200 million	£200 million	£200 million
Annual interest costs (£ million)	£5.5–£6.2 million	£6.6–£7.4 million	£7.4–£8.2 million	£8.0–£8.9 million	£8.3–£9.2 million	£8.6–£9.4 million

Note that the Housing Business Case (R15/2013) fully provides to meet the cost of borrowing from rental income at higher rates (a prudent 5% was assumed) than are presently achieveable.

Tenor Considerations

A range of factors will influence which tenor(s) are deemed to be most appropriate.

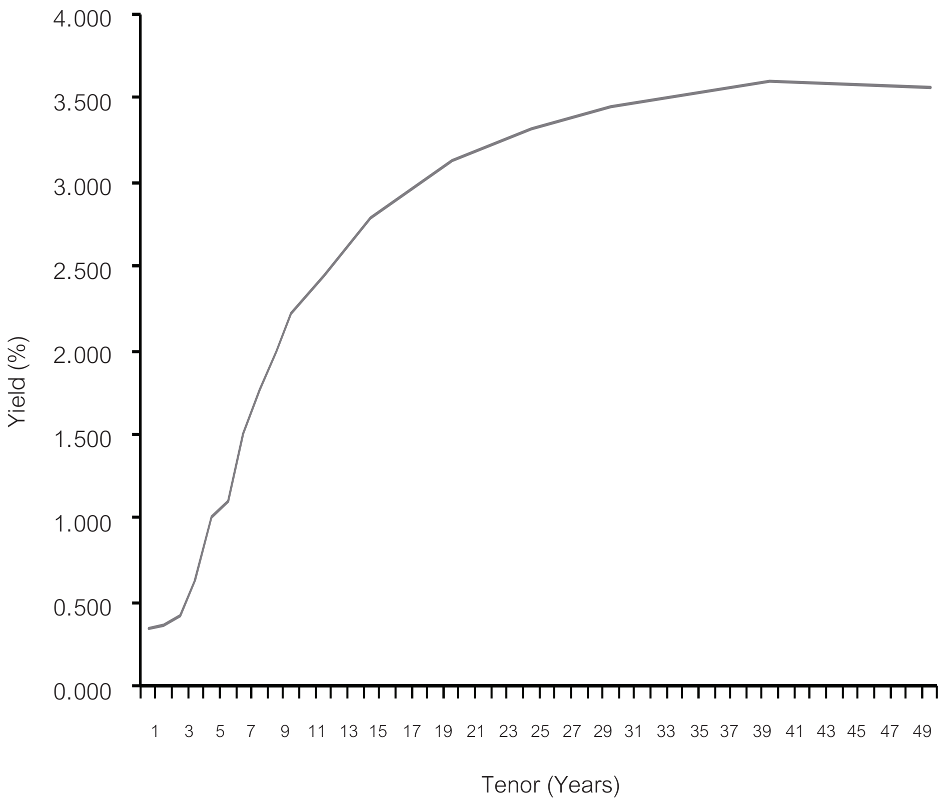
Bonds are priced with reference to an underlying benchmark rate. In the Sterling market this benchmark rate is the Gilt yield at the maturity that most closely matches the maturity of the bond being priced.

Gilt yields change constantly as they are very liquid instruments that are traded very frequently and in high volumes. The yield of Gilts across a range of maturities (the yield curve) is shown in the chart below. Please note that this curve changes constantly according to market conditions.

In order to recompense investors in fixed interest instruments for investing their capital for a longer period of time, the longer the tenor of an instrument, the higher the coupon (in general). Therefore opting for a longer tenor instrument will tend to translate into a higher coupon. This relationship between tenor and yield can be seen in the Gilt yield chart, however the difference reduces at the longer end of the curve.

Investor appetite will vary across the range of tenors. Generally, lower credit quality issuers in a would typically only find support from investors for issuances at shorter maturities. Strong credits that will be in existence far beyond the life of the bond with a reasonable level of certainty like the States of Jersey, are able to access longer maturities.

FIGURE 49 – THE UK GILT YIELD CURVE



Investors will also consider the liabilities that they are seeking to match with the income from the bond coupons. Many bond investors are insurance or pension companies with an exposure to long term liabilities. Therefore they will seek to hold an allocation of longer tenor assets to match their long tenor liabilities.

There are relatively few long tenor bonds issued when compared to more common tenors around the ten year mark. Therefore new supply at this end of the yield curve gives investors an opportunity to diversify their current holdings.

PECRS, JTSF and the CIF could potentially invest in a bond issued by the States of Jersey as part of their managed portfolios. The tenor requirements of these funds, which are driven by the liabilities they are looking to match, would also need to be considered. Independent investment advice from Mercers and Aon Hewitt is provided to these Funds. However, the Bonds would be publicly traded and PECRS, JTSF and CIF would have no obligation to hold them but could make a commercial choice based on independent advice.

We would expect strong support for a longer tenor offering for the States of Jersey. An example of a recent long tenor debut Sterling bond that received very strong support was the £350m issuance from Cambridge University in October 2012. The deal was for 40-year notes which were rated Aaa/stable by Moody's which priced at Gilits+60bps.

The proposed use of borrowing through the issuance of a public rated bond to meet the spending needs of the three major capital projects is limited to £250m for housing purposes.

Indexation Considerations

There is a market for public bonds with a repayment profile linked to inflation indices.

Issuing index linked debt allows issuers to match repayment obligations to index linked cash inflows.

The market for index linked government debt is well developed for the largest and most frequent issuers. However index linked bonds from debut and smaller issuers are extremely uncommon.

Of the smaller high grade sovereign nations detailed in the table below, none have inflation linked bonds outstanding. In comparison, only 17% of the total amount of all UK government bonds are index linked.

FIGURE 50 – SMALLER JURISDICTIONS TEND NOT TO ISSUE INDEX LINKED BONDS

	Bonds outstanding (Sterling equivalent)	% nominal	% index linked
Isle of Man	£260m	100%	0%
Bermuda	£610m	100%	0%
Hong Kong	£5,419m	100%	0%
Singapore	£42,209m	100%	0%
United Kingdom	£1,237,384m	83%	17%

As there is inherent protection against certain risks in an index linked bond, the rewards tend to be equally reduced with index-linked bonds usually offering very low returns. As a result, the investor pool for index-linked instruments is small and it is only the largest, most prolific, well-known issuers that are able to access the small index linked investor base.

Ernst & Young advise that a lower risk option for the States of Jersey would be to target a much wider pool of potential investors through a public bond.

States of Jersey Funds

Borrowing from external sources is not the only option for the States. The States has Funds of its own that are presently invested almost entirely off-Island. There is scope for Funds, in accordance with their own investment strategy, to invest in projects that are on-Island and that have a risk and return profile consistent with the Fund's own investment strategy.

The States of Jersey has a number of funds each with its own legal framework, defined purposes and governance arrangements. These funds include: The Common Investment Fund (in which both the Social Security Reserve and the Strategic Reserve are invested), The PECRS Pension Fund and the JTSF Pension Fund. These Funds amount to around £4 billion in total.

Each of these Funds has its own published Investment Strategy and has investment advice on the development of that strategy from consultants. Mercer, for PECRS and JTSF and Aon Hewitt for The Common Investment Fund. The investment strategies are implemented by the States Treasury.

Each of these strategies has a strategic allocation to traditional asset classes such as government and corporate bonds and equities and also has an allocation to alternative investments such as property and infrastructure. To date this £4 billion has been invested all over the world: in sovereign and sub sovereign government bonds and corporate bonds with high credit ratings and in UK and global equities.

It makes financial sense to all parties to give these Funds the option of a direct infrastructure investment in Jersey with a long term duration at a market rate of interest. It is important for the independence of these Funds that this is an option, not an obligation. This could help reduce the costs to the public purse and be of no detriment to these Funds providing an interest rate and terms are agreed that the Funds' independent investment advisers (Aon Hewitt and Mercer) are satisfied with and that the interests rates provide fair value and an appropriate balance between risk and return.

This option has already been used successfully to provide funding to Jersey organisations that are established with their own constitutions and operate independently of the States. For example, the Parish of Trinity has an investment of £6 million from the Currency Fund to facilitate the development of affordable homes in the Parish. Legal agreements, developed for Treasury by the Law Officer's Department, are in place to set out the terms for the investment. The terms include the purpose of the investment, the rate of return and the repayment terms. In this instance the investment was made from the Currency Fund. This borrowing will be repaid by Trinity by 2016 or sooner and the Parish will benefit from new affordable housing that would otherwise have cost substantially more.

The Table below sets out some of the States' major Funds and gives an indication of the amounts that could be made available for infrastructure investment. These are indicative only.

The proposed use of infrastructure investment to meet the spending needs of the three major capital projects is limited to an investment in the Liquid Waste Strategy of £32m from the Currency Fund.

FIGURE 51 – THE STRATEGIC ALLOCATION TO ALTERNATIVES IN STATES OF JERSEY FUNDS (INCLUDES INFRASTRUCTURE)

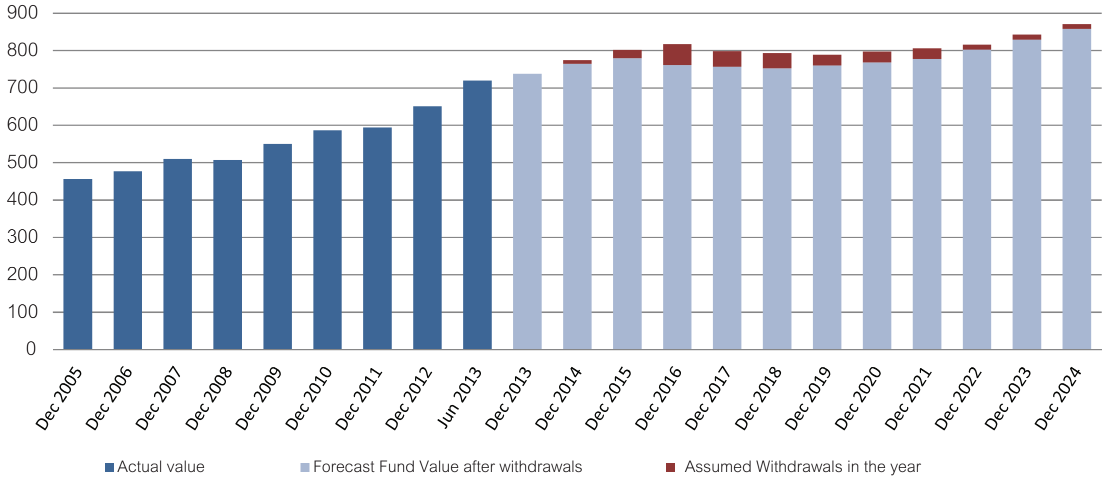
	Strategic Reserve £'m	Stabilisation £'m	Social Security (Reserve) £'m	Health Insurance Fund £'m	Currency Fund £'m
Fund Balances as at:					
31.5.13	£718.0	£1.1	£1,101.0	£76.3	£88.4
31.12.12	£651.0	£1.1	£962.1	£70.1	£90.5
Amount of money held not for investment (i.e. cash buffer)					£2.0
Current Investment Strategy (R.117-2012 published 01.10.12)					
Equities	50%		80%	40%	20%
Alternatives (1) (2)	10%		10%		60%
Bonds	40%	80%	10%	45%	10%
Cash		20%		15%	10%
	100%	100%	100%	100%	100%

Note: (1) Alternative investments in the Strategies are defined to include Infrastructure Investments.

Note the Housing Transformation project in relation to Financing approved by the States says that, £40m would be funded by an Internal Borrowing facility (R.15-2013 and R.132-2011) at 4% per annum, 20 years and the rest by way of external financing (R.15-2013). The Proposition within this Report now recommends funding all of the housing requirement from external borrowing through the issuance of a public rated bond with the debt, to be repaid from the rental income generated from the new properties.

The third possible source of funding for the three major capital schemes is the use of existing States' resources. This Report proposes that the funding for the hospital scheme of an estimated £297 million to be spent over the years 2014 to 2024 is drawn down from the Strategic Reserve Fund thereby meeting the cost of the hospital from the investment returns on the Fund. This means the Hospital project can be met with no new cost to the tax payer and without incurring debt. The hospital would be paid for in full by the time it was completed. The advantages of this are that by the time the hospital is built, the scheme can be fully funded with no new cost to the taxpayer and without the need for borrowing. The hospital costs would be fully met over the 10 years from the Strategic Reserve and leave no debt for future generations. The chart below illustrates how this would work and subsequent charts illustrate the sensitivities, showing what happens if investment returns are higher or lower and what if the spending actually occurs over a shorter 5 year time period rather than 10 years.

FIGURE 52 – PROJECTED STRATEGIC RESERVE FUND BALANCE (£'M) ASSUMING 5% INVESTMENT RETURN AND DRAWN DOWN OF £297M FOR THE HOSPITAL



Strategic Reserve Balance

When considering this proposal, State Members may find it helpful to see the history of the Strategic Reserve Fund, and the amounts of Capital injected to create and build the Fund and the investment returns generated on it. The Tables and data below may assist.

The Strategic Reserve was created in 1986 with an initial capital injection of £10 million. In the years since the inception of the Fund a further £167 million has been transferred in and capital withdrawals totalling £60 million have been made, giving a net capital position of £117 million (Figure 53, see overleaf).

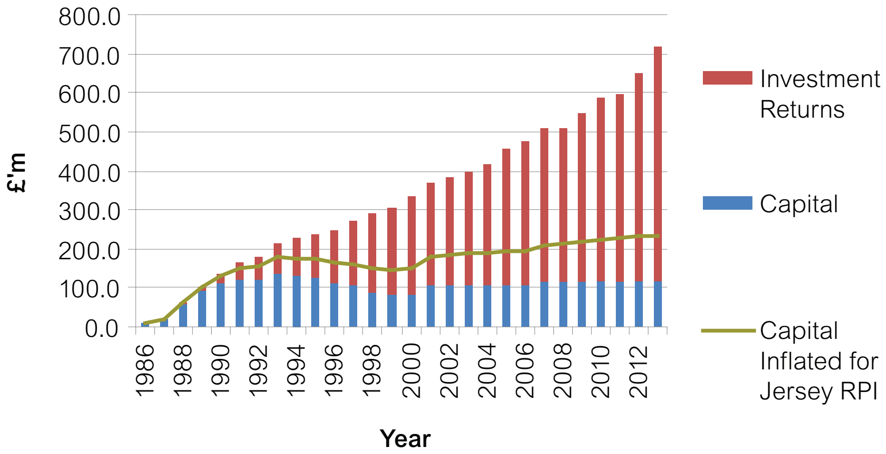
FIGURE 53 – STRATEGIC RESERVE 1986–2013 (AS AT 31ST AUGUST) CAPITAL MOVEMENTS

Year	Capital In £	Capital Out £	Net Capital Movement £	Cumulative Capital £
1986	10,079,392	-	10,079,392	10,079,392
1987	10,000,000	-	10,000,000	20,079,392
1988	40,000,000	-	40,000,000	60,079,392
1989	30,000,000	-	30,000,000	90,079,392
1990	20,000,000	-	20,000,000	110,079,392
1991	10,000,000	-	10,000,000	120,079,392
1992	-	-	-	120,079,392
1993	17,095,832	-	17,095,832	137,175,224
1994	-	(5,000,000)	(5,000,000)	132,175,224
1995	-	(7,000,000)	(7,000,000)	125,175,224
1996	-	(15,000,000)	(15,000,000)	110,175,224
1997	-	(5,000,000)	(5,000,000)	105,175,224
1998	-	(17,500,000)	(17,500,000)	87,675,224
1999	3,000,000	(10,500,000)	(7,500,000)	80,175,224
2000	4,000,000	-	4,000,000	84,175,224
2001	23,000,000	-	23,000,000	107,175,224
2002	-	-	-	107,175,224
2003	-	-	-	107,175,224
2004	-	-	-	107,175,224
2005	-	-	-	107,175,224
2006	-	-	-	107,175,224
2007	10,000,000	-	10,000,000	117,175,224
2008	-	-	-	117,175,224
2009	-	-	-	117,175,224
2010	-	-	-	117,175,224
2011	-	-	-	117,175,224
2012	-	-	-	117,175,224
2013	-	-	-	**117,175,224**
TOTAL	**177,175,224**	**(60,000,000)**	**117,175,224**	

The investment returns on the Strategic Reserve since its establishment in 1986 amount to £599 million over the value of capital invested. The total balance of £716 million as at 31st August 2013 is therefore made up of £117 million in principle (capital) and £599 million of investment returns (interest).

If the capital of £117 million within the Strategic Reserve Fund were increased in real terms, in line with Jersey inflation, the capital element would be £230 million. Figure 54 illustrates this.

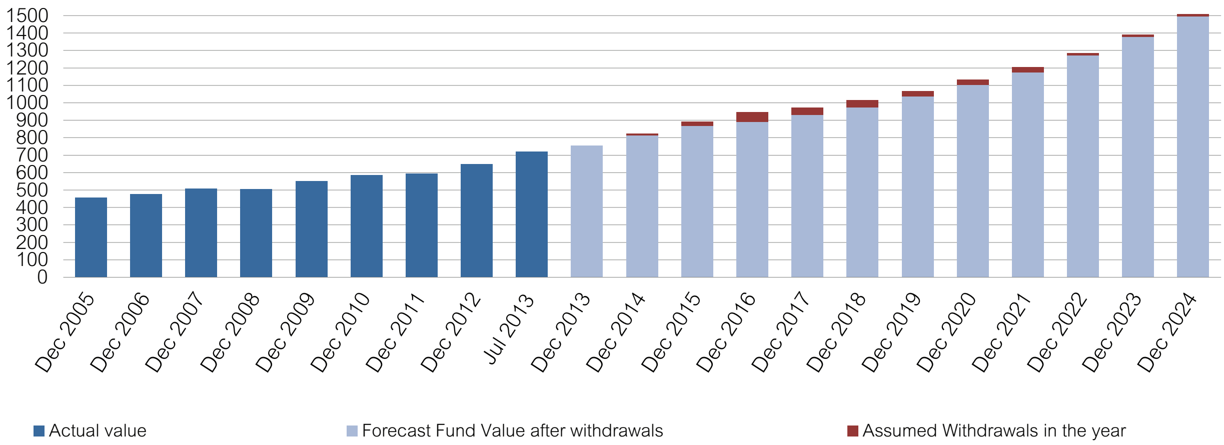
FIGURE 54 – STRATEGIC RESERVE CAPITAL AND INVESTMENT RETURNS



DIFFERENT SCENARIOS FOR THE STRATEGIC RESERVE

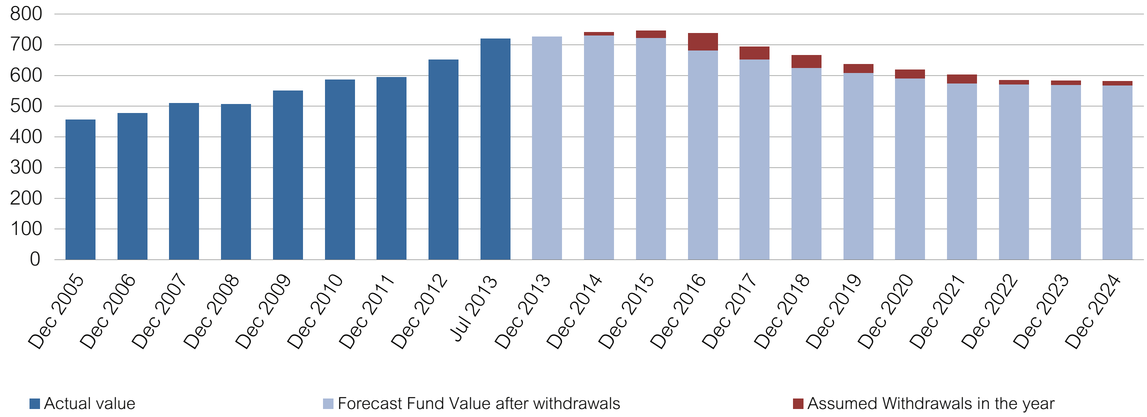
In July 2010 the Strategic Reserve balance was £550m and in July 2013 it is £720m – the compound average annual growth is 9.4% per annum. If this rate of growth were to continue and Treasury would not advise making a decision based on such ambitious investment targets being achieved, then the Strategic Reserve Fund would stand at the levels shown in the chart below. This is based on actual performance in the last three years but it is included only for illustration. Treasury recommends the decision to be taken on a prudent assumption of an average of 5% returns.

FIGURE 55 – PROJECTED STRATEGIC RESERVE FUND BALANCE (£'M) ASSUMING 9.4% INVESTMENT RETURN AND DRAWN DOWN OF £297M FOR THE HOSPITAL



At the other end of the spectrum, if the Strategic Reserve Fund achieved only a long term average of 2% returns and £297m were drawn down to fund the hospital, the balance by 2024 would still be close to £600m and still well above the capital values inflated for Jersey RPI.

FIGURE 56 – PROJECTED STRATEGIC RESERVE FUND BALANCE (£'M) ASSUMING 2% INVESTMENT RETURN AND DRAWN DOWN OF £297M FOR THE HOSPITAL



The final sensitivity graph below shows what happens if the 5% annual growth assumption is used, but the hospital project proceeds much faster – in fact at twice the planned rate. The £297m for the hospital would then be drawn down over five years rather than the estimated ten years.

FIGURE 57 – PROJECTED STRATEGIC RESERVE FUND BALANCE (£'M) ASSUMING 5% INVESTMENT RETURN AND DRAWN DOWN OF £297M (ACCELERATED TO 5 YEARS) FOR THE HOSPITAL

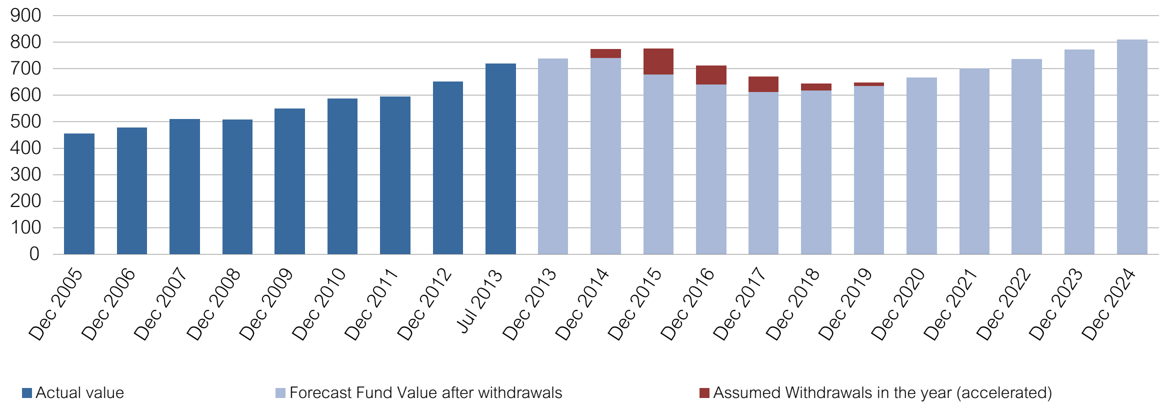


FIGURE 58 – HOUSING BORROWING – INDICATIVE COSTS

Funding method (which includes the issuance costs)				
- Amount to Borrow	£207/250m	£207/250m	£207m	£43m
- Life of the bond	20 years	30 years	20 years	20 years
- Type of bond	Public bond with rating	Public bond with rating		
- Gilt rate (valid 02/07/13)	3.18%	3.53%		
- estimated coupon (valid 02/07/13)	3.88%	4.33%	3.88%	3.88%
- issuance date			2014	2018
Annual costs – interest costs				
first 10 years			8,031,600	1,001,040
year 11–20			8,031,600	1,668,400
year 21–24				1,668,400
year 25–30			–	–
year 31–34				
Total cost of 20/30 years			**160,632,000**	**33,368,000**
Average Annual charge to sinking fund (assumed 4.0% return pa, zero year 1 and the final year)				
first 10 years			3,710,000	
year 11–20			12,163,961	3,205,447
year 21–24				
year 25–30		–	–	
year 31–34		–	–	
Total cost of 20/30 years			**158,739,610**	**32,054,470**
TOTAL COST PER ANNUM				
first 10 years			11,741,600	1,001,040
year 11–20			20,195,561	4,873,847
year 21–24			–	1,668,400
year 25–30			–	–
year 31–34			–	–
Total cost of 20/30 years			**319,371,610**	**65,422,470**

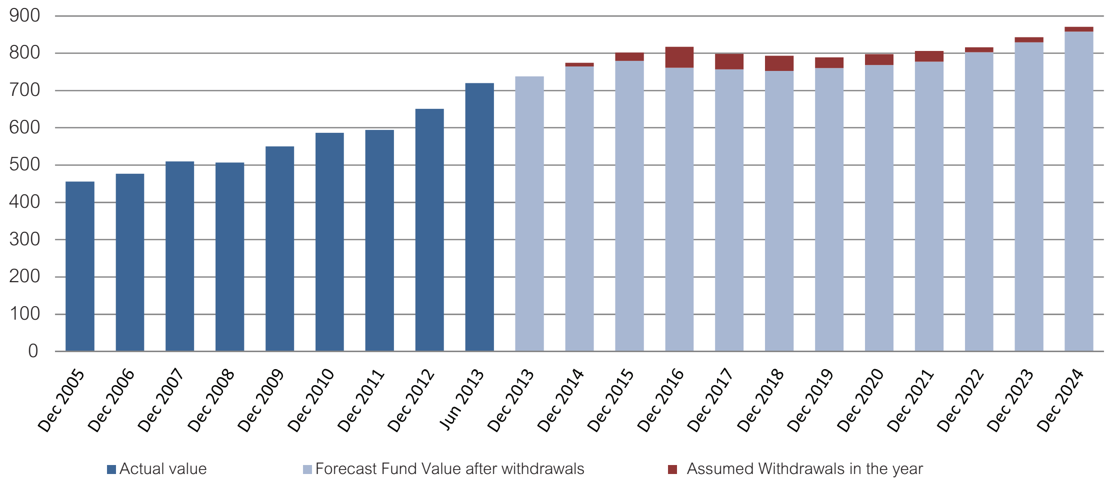
Notes

The Housing financial model currently assumes they can draw down the monies as they require and pay interest and also capital repayments. The Housing financial model is based on a 20 year repayment basis. Housing will draw on the funds raised from the bond issuances as and when they require it. Interest will only be payable by housing when funds are drawn down. Housing will pay into the sinking fund from year 9 onwards at variable amounts, but calculations have been prepared to ensure the funds are invested in the sinking fund to ensure full and final payment upon each maturity for each bound issued. If a bond is raised for 30 years, whilst it is not inline with housings model, there are would be additional interest cost however it provides the opportunity of cheaper financing for an extra 10 years.

15. Summary Of Proposals For Funding The Three Major Capital Projects

Hospital Project – £297 million from the Strategic Reserve Fund Drawn As Required

FIGURE 60 – PROJECTED STRATEGIC RESERVE FUND BALANCE (£'M) ASSUMING 5% INVESTMENT RETURN AND DRAWN DOWN OF £297M FOR THE HOSPITAL



The proposed funding route means that:

- The Hospital costs would be fully met over the 10 years of development from the Strategic Reserve;
- There would be no debt for future generations;
- There would be no new cost to the taxpayer;
- The cost of the Hospital will be funded from the Investment Returns of the Strategic Reserve Fund; and
- The funding remains in the Strategic Reserve until it is needed and is fully invested so as to maximise investment return and minimise cost.

Housing Project – £250 million by Public Rated Bond

Ernst & Young advise that of the external debt markets open to the States of Jersey, the public bond market is likely to provide the tightest pricing for long term debt capital.

Accessing the Sterling public bond market (with a public credit rating) offers a sensible and cost effective financing route for housing purposes and is recommended.

- Sterling bonds are priced in the public bond market with reference to a credit spread above UK Gilts, which are currently at historic lows.
- A public rating will increase transparency, give investors confidence, and allow a robust pricing argument to be constructed.
- The Housing Business Case (R15/2013) assumed that external borrowing would be used and fully provides for meeting the costs of principal and interest.
- The costs of repayment of the debt would be met from the housing rental income stream.
- The new Housing Company would have new assets (housing) on its balance sheet to offset the liabilities (debt).

Liquid Waste Project – £29 million through Infrastructure Investment and Use of Existing Resources

The proposed sources for liquid waste are set out in the Table below.

FIGURE 59 – FUNDING SOURCES FOR LIQUID WASTE

	2013 £'m	2014 £'m	2015 £'m	2016 £'m	2017 £'m	2018 £'m	2019 £'m	2020 £'m	TOTAL £'m
TTS Rolling Vote	–	4.0	–	4.0	4.0	–	–	–	12.0
Main Capital Programme	–	3.1	–	6.7	7.4	12.2	1.1	–	30.5
Consolidated Fund	–	3.0	–	–	–	–	–	–	3.0
Infrastructure investment from currency fund	–	–	21.2	7.8	–	–	–	–	29.0
Existing resources	0.5	–	–	–	–	–	–	–	0.5
Total required	**0.5**	**10.1**	**21.2**	**18.5**	**11.4**	**12.2**	**1.1**	**–**	**75.0**

The funding sources proposed and recommended for liquid waste are:

- a targeting of the existing rolling capital vote (£12m);
- an allocation within the traditional main capital programme (£34m); and
- an investment from the Currency Fund allocation to infrastructure (£29m) with interest and principle to be repaid by TTS from existing resources and operational cost savings generated by the new infrastructure.

The funding route means that:

- there is no external debt;
- the internal borrowing benefits the Currency Fund (say a 4% return against a cash return of only 0.8%);
- the borrowing cost and risk to TTS is minimised;
- there is not new cost to the taxpayer;
- there is no external debt added to the States' Balance Sheet; and
- it is an affordable option for TTS because the new infrastructure is more energy efficient and is cheaper to run.

16. Appendix A

Better Health and Social Services

Better Health and Social Services

Jersey's Future +Hospital

Outline Funding Strategy

and proposals for a detailed Feasibility Study

A New Way Forward

The Health and Social Services Report and Proposition P.82/2012, approved by the States Assembly on the 23rd October 2012, sets out the vision of an integrated care model and a programme of change that will meet the challenges facing the Island's future Health and Social Services.

Central to the development of this vision is the need to have an acute general hospital which is fit for purpose, capable of sustaining the acute care provision requirements for the population and complements the integrated care strategy being developed for Jersey.

Consultation has shown that Islanders want Health and Social Services that are:

'Safe' – while many health interventions involve inherent levels of risk, that patients and service users should not be exposed to an undue level of risk.

'Sustainable' – that services should be organised in a way that is not vulnerable to change in the short term.

'Affordable' – that the model of services represents value for money relative to other potential model.

P.82/2012 makes clear that new hospital capacity will be required within 10 years.

Existing Hospital – Condition and Development Potential

WS Atkins were appointed to review the condition and development potential of the existing General Hospital. Their report confirmed the following:

- The total floor area of the combined hospital buildings (circa 38,500m2) is about 60% of that needed for a full new hospital to modern standards (63,600m2).
- A condition assessment carried out in 2008 assessed the majority of the building as being in category C or D – i.e. needing significant investment or replacement.
- Poor configuration and/ or condition meant that some of the existing buildings have limited potential for clinical use or development in a future hospital.
- The layout of the hospital means that there is little opportunity to intensify uses on the current plot and any development would need to be in a phased manner.

WS Atkins concluded that a complete redesign and increase in the size of the existing Hospital is required, not only to meet the future acute clinical needs of the growing population of Jersey, but also to address the increase in space standards required to meet current best clinical, spatial and operational practices.

100 Single Bed Rooms

FIGURE 61 – EXISTING HOSPITAL – 6 BED WARDS

21st Century Theatres

FIGURE 62 – EXISTING HOSPITAL – 1980S THEATRES

21st Century Laboratories

FIGURE 63 – EXISTING HOSPITAL – 1970S LABORATORIES

Ageing Population and Activity Analysis

WS Atkins reviewed hospital activity, service development plans and proposals for delivering more health services in the community to establish the scale of future hospital capacity required.

Assuming 2011 Census projections and that proposals within P.82/2012 are successfully implemented, new hospital capacity of circa 300 beds will be required.

Pressures on bed numbers will grow before new hospital capacity is available such that by 2017 up to 50 additional beds will be required to avoid permanent bed crisis.

Site Search

Jersey Property Holdings were commissioned to undertake a spatial assessment for new Hospital capacity to inform P.82/2012.

- The Planning and Environment Geographical Information System was employed for the subsequent site search.

- A cross-Departmental Officer group reviewed 24 potentially suitable sites and identified a long-list of 11 sites for review by WS Atkins International – a respected hospital master-planning consultant.

- All sites of sufficient footprint (18,000m2) within or adjacent to the Built Up Area were reviewed against set criteria including green and brownfield sites.

- Potential sites suggested by the Minister for Planning and Environment were also reviewed.

- Potential sites were drawn up and evaluated by WS Atkins using cost, benefit and risk criteria. WS Atkins recommend a short-list of 3 sites.

The Ministerial Oversight Group for health transformation, having considered all of the alternatives, accepted the Officer recommendation that the existing general hospital site offered the best location for key investment in future hospital capacity.

Model of Care

Architects appointed to develop the future hospital identified that there is insufficient footprint on the current hospital site to develop all of the new services needed.

Planning restrictions are in place – for example on the listed Granite Building -and massing restrictions limit the ability to develop the larger building needed.

Investing in one site would also not maximise the benefit of the available investment and would result in a lengthy complicated construction programme that would cause considerable inconvenience to patients.

A new model of care is therefore proposed that would separate emergency / in-patient overnight care from out-patient day care.

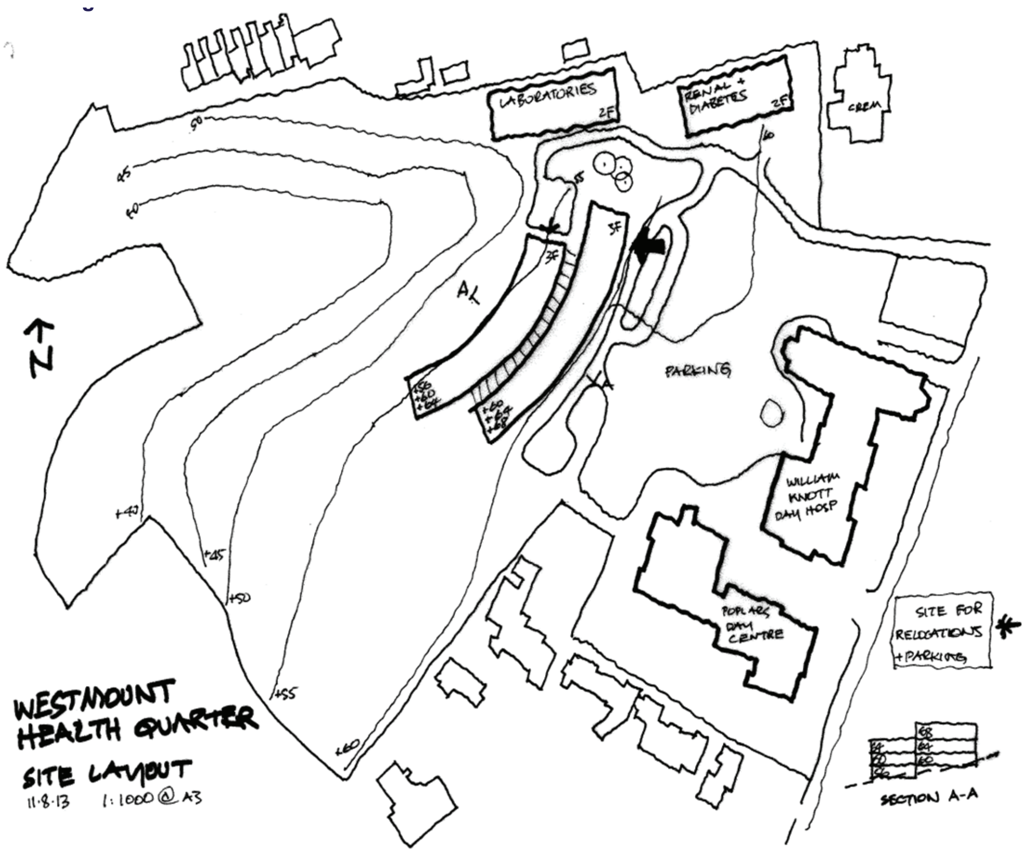
A brand new out-patient building would be developed at the Overdale Hospital integrated with the existing rehabilitation and social services to form a Westmount Health Quarter.

This would free up vital space to allow new theatre, bed, Accident and Emergency and children's bed capacity at the existing hospital site.

Westmount Health Quarter

The design of the Westmount Health Quarter is for a modern, high quality out-patients building within the excellent healing environment at Overdale. The existing Westmount Health Centre, William Knott and Poplars buildings will be retained.

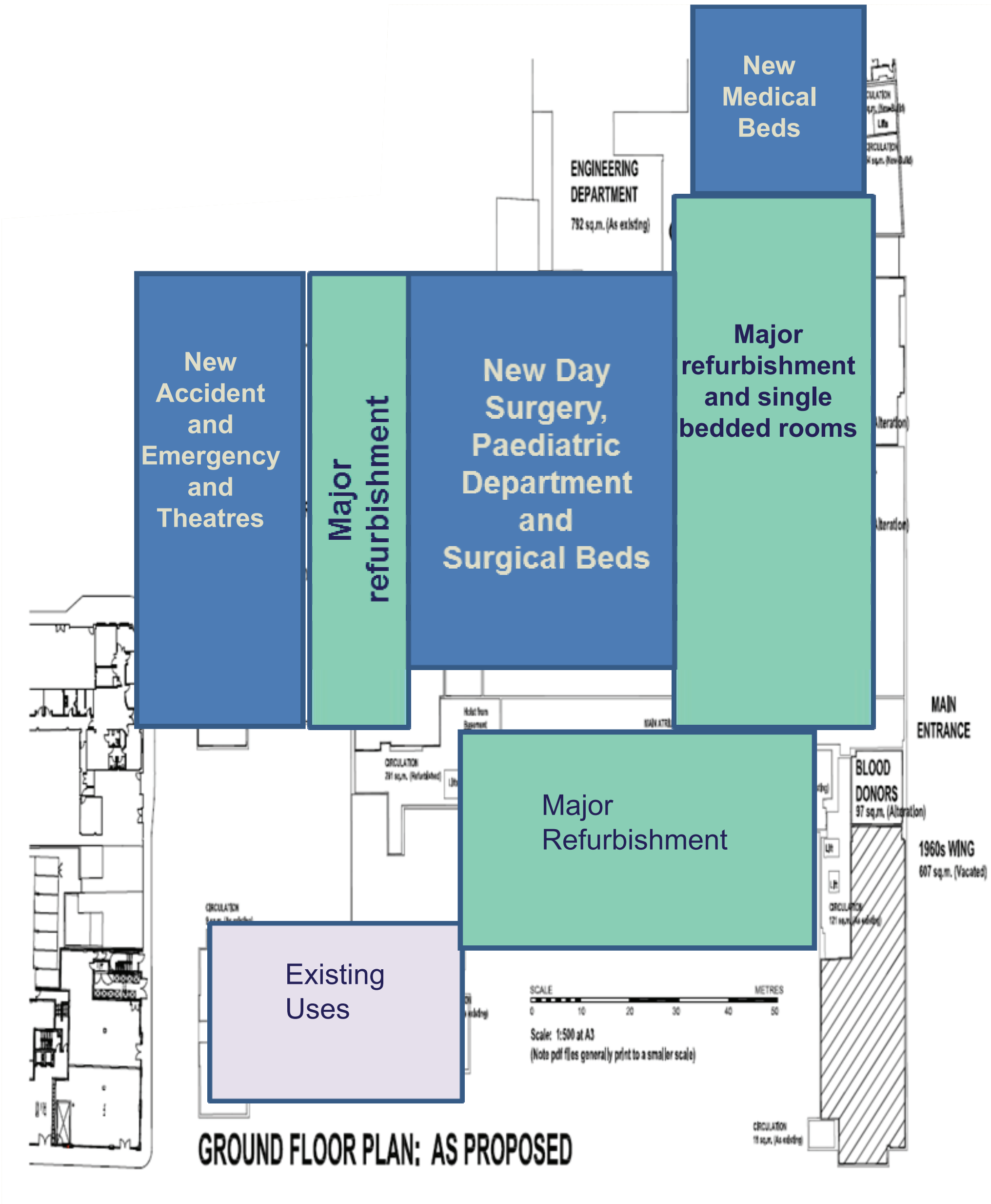
FIGURE 64 – WESTMOUNT HEALTH QUARTER – SITE LAYOUT



St Helier General Hospital

The proposal for the future St Helier General Hospital is for a large new build development on the western perimeter (Overdale) and extensive sensitive refurbishment of those existing buildings suitable for continued hospital use.

FIGURE 65 – AN INDICATION OF THE MIX OF NEW BUILD AND REFURBISHMENT WORKS AT THE HOSPITAL



Funding

A completely new hospital development on the current site would be unaffordable at circa £462m.

Therefore a £297m target project budget has been set as one that was prudent in the current economic conditions.

The new Westmount Health Quarter and St Helier General Hospital can be developed within that budget.

Funding has been identified for a radiographic department within the St Helier General Hospital meaning cancer patients can receive treatment on island.

Proposals for short term theatre and bed capacity have been funded and some social services functions at Overdale will also be re-provided within this funding envelope of £297m.

17. Appendix B

Housing refurbishment and new build projects

The Housing business case refers to refurbishment and new build projects. These are listed below along with the estimated total costs from R015/2013. For comparison purposes, the projects included at Outline Business Case stage are also included. Individual project costs are not shown as this is considered to be commercially sensitive. Costs are indicative and are subject to change, particularly for projects for which feasibility studies have not yet been performed. Costs will be managed by the Housing Company as each of the projects is progressed.

FIGURE 66 – HOUSING SCHEMES PLANNED FOR FUNDING FROM BORROWING OF £250M

Refurbishment Costs	OBC stage £000s	FBC stage £000s
Repayment for Pomme D'or scheme		
Le Squez - Phase 3b		
Victoria Cottage Homes (new build project at OBC stage)		
Jardin des Carreaux		
La Collette		
Journeaux Street Intensification		
Hampshire Gardens Convent Court Caesarea Court		
De Quetteville Court High Rise		
Hue Court High Rise		
Osborne Court		
Refurbishment Costs	**42,274**	**54,257**
New build costs on existing housing sites or sites covered by P40/2012	**£000s**	**£000s**
Repayment for Le Squez - phase 2a and 2b		
Le Squez – Phase 2c		
Journeaux Street, 2–4		
Lesquenade 1		
Ann Court (project being undertaken by a Housing Trust)		
Le Squez - Phase 4		
Le Squez - Phase 5, 7, 8		
Le Squez - Phase 6, 9, 10, 11 and 3a		
Victoria Cottage Homes (refurbishment project at FBC stage)		
Lesquenade 2		
Fields 516, 517 and 518 St Saviour		
La Collette – Block B and C		
La Collette – Blocks C, D and F		
New build costs	**89,664**	**116,060**
Total refurbishments and new build costs	**131,938**	**170,317**
New build costs on other social housing sites	**£000s**	**£000s**
Former Le Coin Site Summerland Site Ambulance Station Site Pine Ridge		
Additional new build costs	–	31,055
Total	**131,938**	**201,372**
Other		6,000
		207,000
Provision for re-zoned sites / Site acquisition		43,000
Total borrowing requirement		250,000

18. Appendix C

FIGURE 67 – SEWERAGE NETWORK

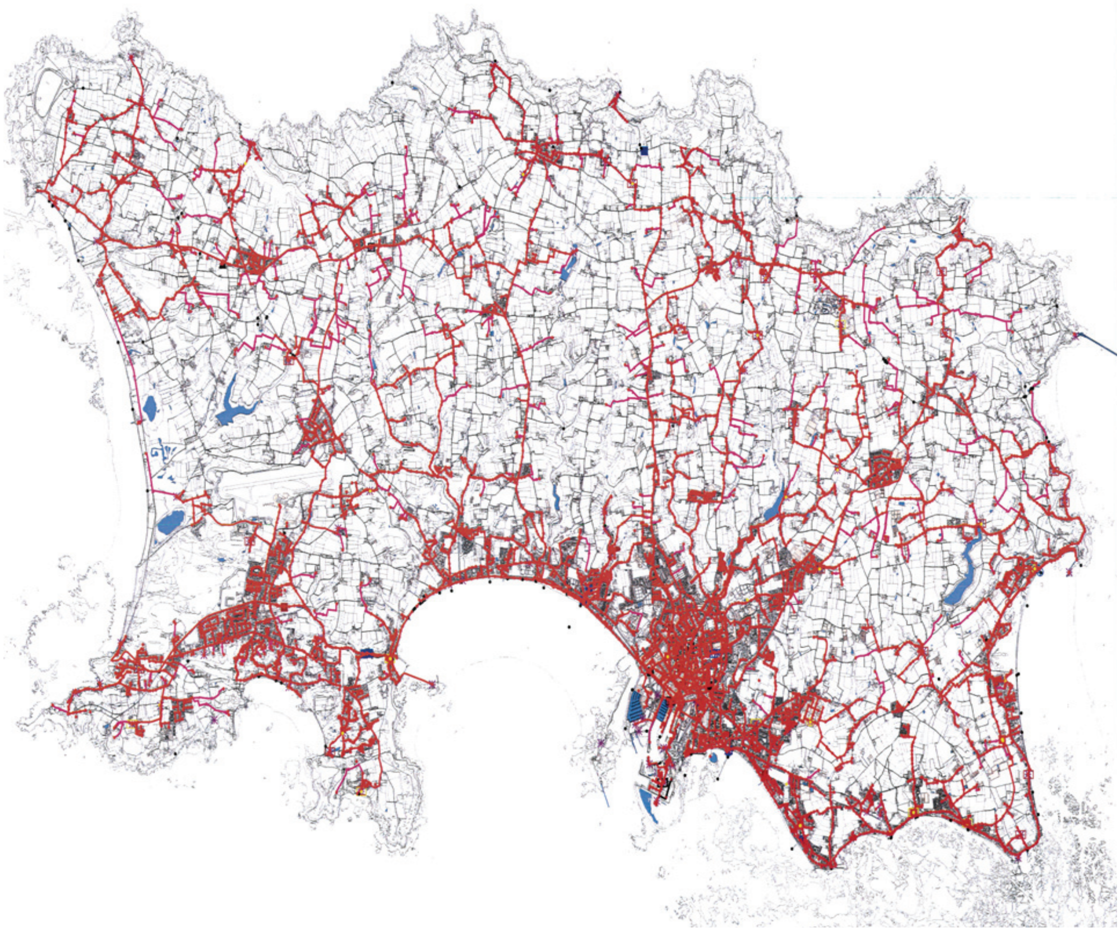


FIGURE 68 – WATER FRAMEWORK DIRECTIVE

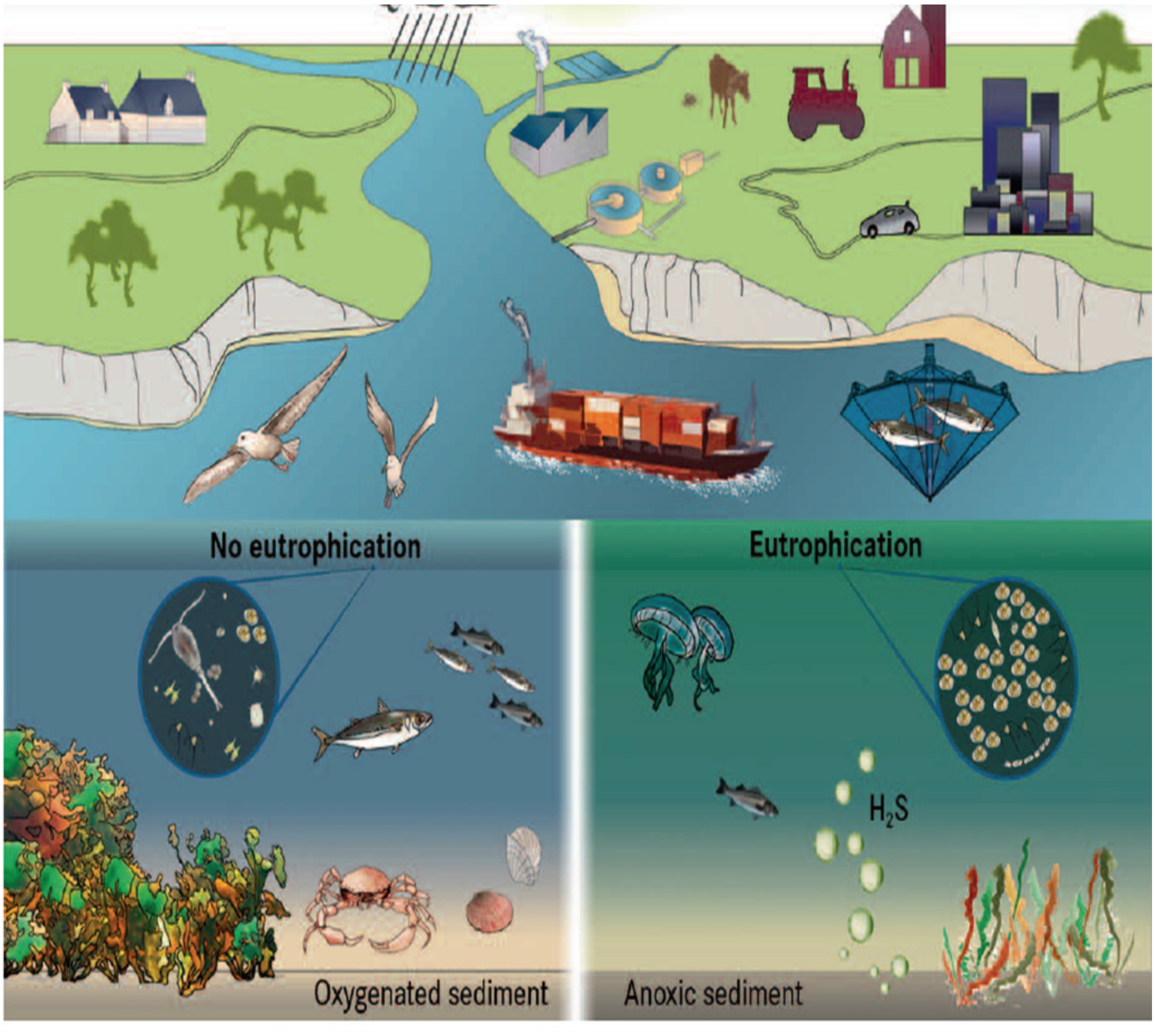


FIGURE 69 – AGEING SEWAGE TREATMENT WORKS

FIGURE 70 – DRIVERS FOR CHANGE

FIGURE 71 – AGEING SEWAGE TREATMENT WORKS

FIGURE 72 – AGEING SEWAGE TREATMENT WORKS

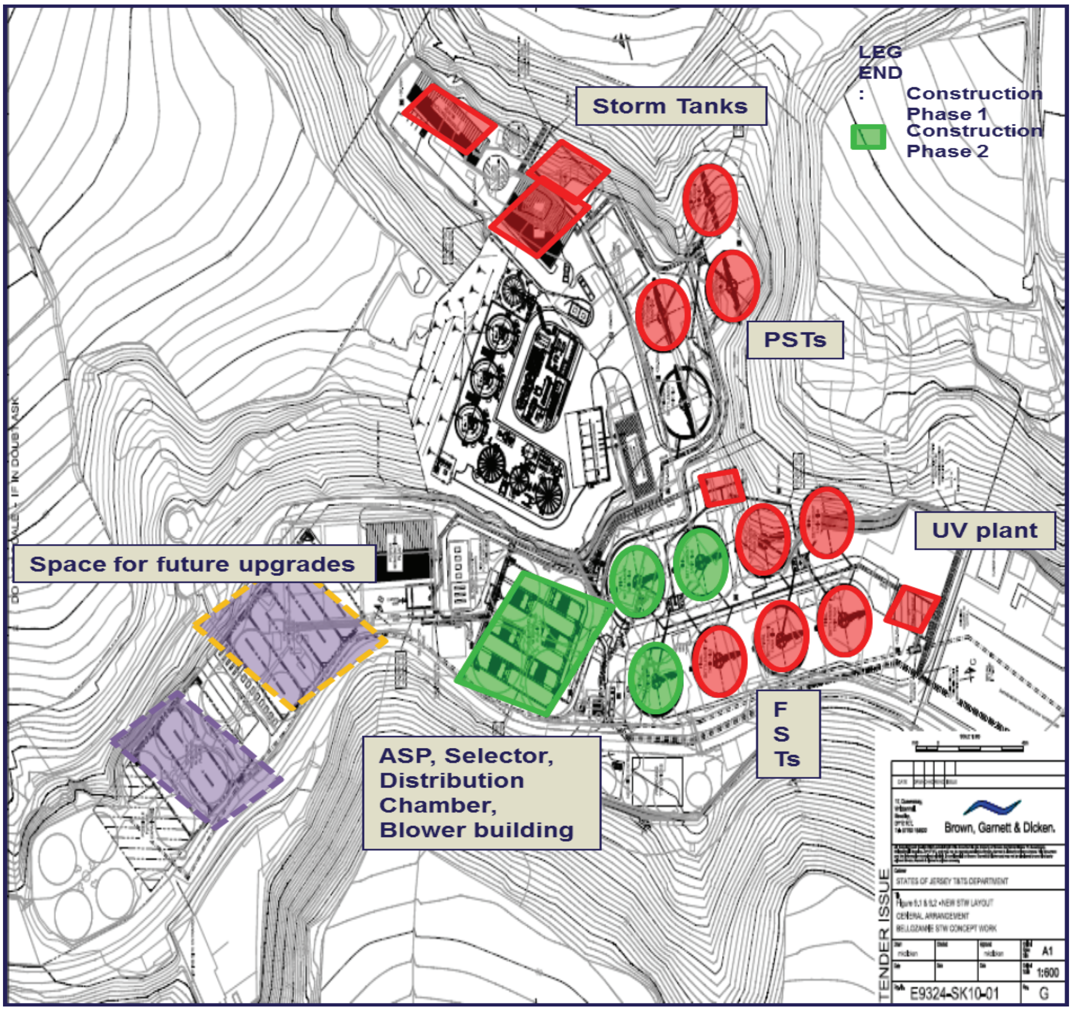
Upgrading the Sewage Treatment Works will Allow For:

- Odour control facilities.
- Higher automation.
- Electricity generation.
- Reduced staffing.
- Additional treatment capacity at the works(over 30%).
- Additional storm sewage storage at the works.

Resulting in: No more storm sewage being discharged via the outfall into St Aubins Bay

FIGURE 73 – EXAMPLES OF NEW, EFFICIENT, LIQUID WASTE INFRASTRUCTURE

FIGURE 74 – POSSIBLE CONFIGURATION OF NEW PLANT AT BELLOZANNE



Challenges

Location – Bellozanne identified as most suitable site. Network diversions to a new location are very costly

Process – Conventional Activated Sludge process which is adaptable for all treatment options

Surface water reduction in foul sewers – releases sewer capacity but not treatment plant size

19. Appendix D – The Steps Involved In Issuing A Public Bond

Strategy Execution – Debt Issuance

Appointing Advisors

There is a small range of advisors that the States of Jersey will need to appoint, in a competitive manner.

The roles for which appointments will be made at the start of the issuance process include:

- Bookrunner(s): Responsibilities are numerous, with main roles including production of investor presentation, arranging road show logistics, marketing to potential investors, bookbuilding and documentation, including the Prospectus (which is the main Offering Document to potential investors).There is unlikely to be a cost benefit to the States of Jersey in appointing bookrunners for more than one bond at a time and they are normally appointed on a deal by deal basis to ensure competitive tenders for each assignment.

- Legal advisor: Responsibilities of legal advisors include the drafting of documentation. Documents that will require legal input include:

  i. The Prospectus, which will be signed off by the appropriate Listing Authority. This is the FSA if a London listing is chosen;

  ii. Subscription Agreement, which is a relatively standard legal agreement between the States of Jersey and the bookrunners, covering the terms on which the bond will be issued and the representations and warranties of all parties;

  iii. Trust Deed, which is a legal agreement with the Trustee, setting out the limit of empowerment to act for the bondholders as a group;

  iv. Agency Agreement, which will be the agreement between the States of Jersey and the Paying Agent; and

  v. Auditors Comfort Letter, which gives the underwriting banks comfort that the Prospectus is accurate. This is usually a standard form letter.

- Legal advisors will be required for both the States of Jersey and the bookrunner(s).

- Paying Agent: Usually one of the bookrunners, who will be responsible for the disbursement of funds in connection with the bond, will act as Paying Agent. The paying agent will receive coupon payments from the States of Jersey, and pass on to the holders of the bonds.

- Trustee: Again, usually one of the bookrunners will take the role of trustee. The trustee sees that bond interest payments are made as scheduled, and protects the interests of the bondholders if the issuer defaults. The trustee is responsible for the registration, transfer and payment of bonds.

- Trustee legal advisor: Legal counsel will be required for the trustee.

- Indicative anticipated costs for the roles that require appointing are shown in section.

Indicative Upfront Costs

There are large number of upfront fees associated with a public bond issuance, and a small number of ongoing fees

Bookrunner fees and credit rating fees on issuance have been calculated assuming a bond size in the region of £200m -£500m.

The other upfront costs, included in the table below, are likely to be in the ranges proposed irrespective of the size of the bond.

FIGURE 75 – INDICATIVE COSTS OF ISSUING A PUBLIC RATED BOND

	Indicative estimate up front costs*	Comments
Bookrunners#	£420,000 – 1,050,000	18 - 21bps of the funds raised is typical, however we will look to reduce through competitive tender. Fee is paid upfront, one-off and shared across all bookrunners
Credit ratings€	£110,000 – 275,000	5.5bps on any bond issuance (3.5bps for S&P and 2bps for Fitch)
Issuers Legal Counsel	£50,000 – 80,000	Subject to a competitive tender. Fixed fee (i.e. not based on quantum raised), required on each bond issued
Bookrunners Legal Counsel	£50,000 – 90,000	Subject to a competitive tender. Fixed fee, required on each bond issued
Trustee and Paying Agent	£3,000 – 5,000	Subject to a competitive tender. Fixed fee, required on each bond issued
Trustee Legal Counsel	£10,000 – 15,000	Subject to a competitive tender. Fixed fee, required on each bond issued
Auditor's Comfort Letter	£5,000 – 8,000	Fixed fee, required on each bond issued
Stock Exchange Listing Fee	£5,000 – 10,000	If the bond is listed in London, this is a one-off fee per bond.
Roadshow and Printing Costs	£5,000 - 10,000	Dependent on scope of roadshow and travelling party. A roadshow will be required with each issuance

*Subject to the States of Jersey's negotiations.

In addition to the upfront costs listed above, there will be a small number of fees which are ongoing for the life of the bond. These include an ongoing assessment fee to the rating agencies of around £32,000 per rating agency and the fee to the Trustee and Paying Agent. These costs can be met from within Treasury's existing resources.

Unlike some other exchanges, the London Stock Exchange does not charge annual fees for listing bonds. This makes a long term bond very cost effective. We have assumed a London listing to maximise liquidity and secondary appetite for the bonds, which ultimately maximises pricing efficiency. Comparable sovereign bonds (UK, Isle of Man) are listed on the London Stock Exchange.

Designing an Invitation to Tender

Designing an Invitation to Tender ('ITT'), alternatively known as a Request for Proposal, and the subsequent assessment of potential bookrunner(s) will be critically important in maximising the marketing channels available to the States of Jersey

We will develop a suggested ITT document to select a bookrunner(s), which will be designed to assess key criteria of representative banks. Factors will include:

- Relevant experience: A demonstrable track record of dealing with sovereigns will be essential, as will evidence of arranging debut capital markets issuances. Ideally your bookrunner(s) would have experience of arranging the debut issuance of a sovereign, although we would not recommend that this be a limiting criteria.

- Size, locations and capability of sales and distribution force: The States of Jersey should target bookrunner(s) that have the ability to reach as wide a potential investor base as possible. This allows the States of Jersey to maximise the order book, create competitive tension amongst investors and increase pressure on the pricing.

- Market research and marketing approach: The bookrunner(s) will need to demonstrate an understanding of the States of Jersey's objectives to be able to best market the issuance. For instance, understanding that oversubscription should lead to increasingly selective acceptance of offers, rather than an increase in the quantum of the bond. The bookrunner(s) should also understand the States of Jersey's desire to maximise offers received rather than selectively managing the investor base ahead of any subsequent issuance.

- Sales strategy, including highlighting who they believe to be key investors: Our view is that, with a well-considered marketing strategy, the States of Jersey's debut issuance is likely to attract significant interest across the investor universe. During the bookbuilding phase, the bookrunner(s) should maintain a dialogue with any investors that the States of Jersey is keen to include, (for example any Jersey based investors to allow for local investment in the States of Jersey) to ensure that any bids received from local investors are such that they are likely to result in allocation. A view on the pros and cons of a States of Jersey fund as an anchor investor will also be sought.

- Views on current market and planned timing of the deal: The conditions of the capital markets and potential timing of issuance will be crucial to ensuring a best deal for the States of Jersey. The ITT will ensure bookrunner(s) present a view and outlook of the credit markets and best timing for the States of Jersey.

- Unique ability to add value to the deal: Any specific unique capabilities of the bookrunner(s) to meet the aims of the States of Jersey. These abilities will be highlighted by the banks as part of their responses to the ITT, with the onus on the banks to present experience or insights which distinguishes them from their competitors.

- Performance in relevant league tables: Comparison and track record against peers to ensure established and experienced bookrunner(s) are appointed.

- Due diligence: The bookrunner(s) would need to comply with the States of Jersey's due diligence process, i.e. providing suitable references, credit checks, contracts etc as detailed in the ITT.

- Fees: Acting as bookrunner to the States of Jersey's debut bond issuance will be a highly prestigious role for bookrunner(s). The fee quote should reflect best value for the States of Jersey.

Bookrunner Roles

To obtain best value for the States of Jersey, we would advise that the number of bookrunners is kept low.

- There is not a linear relationship between funds raised and the number of bookrunners. It is usual to have more than one bookrunner, but usual to keep the group small to ensure appropriate focus.

- The dynamic between issuers and relationship banks tends to have a bearing on how roles and responsibilities are allocated on a bond issue. As the States of Jersey does not have any significant borrowings, this dynamic will not be significant therefore we would advise appointing a small, focused group of banks.

- A robust tender process will identify the banks with the strongest capability in relation to the States of Jersey's requirements. A £400-500m Sterling bond issue for a high investment grade credit rating will be well within the core competency of many investment banks and therefore there is no requirement to appoint a large group of banks in order to ensure adequate take up or a liquid market in the securities.

FIGURE 76 – STERLING BOND BOOKRUNNER LEAGUE TABLE (BY AMOUNT, JAN 2012 TO FEB 2013)

Rank	Bookrunner	Amount (£bn)	Number of issues
1	Barclays	19.1	120
2	HSBC	17.9	118
3	Deutsche Bank	17.0	100
4	RBS	16.2	125
5	Lloyds TSB Corporate Markets	10.8	72
6	RBC Capital Markets	10.0	84
7	UBS	8.5	49
8	Goldman Sachs	6.6	33
9	Credit Suisse	6.1	34
10	Banco Santander	5.9	34
11	BNP Paribas	5.1	37
12	Morgan Stanley	4.7	15
13	Nomura	4.0	14
14	JP Morgan	3.9	27
15	Bank of America Merrill Lynch	3.8	25
16	Citi	3.1	19
17	Société Générale	1.4	8
18	Credit Agricole	1.3	5
19	Deutsch Pfandbriefbank	1.1	2
20	National Australia Bank	0.6	6

It is common market practice in the investment grade Sterling market for two bookrunners to be appointed. The main responsibilities of the bookrunners will be documentation and investors presentations / road show organisation – splitting of these roles and responsibilities should occur as follows:

- A bank should be mandated as Lead Bank in relation to documentation -it will be their role to coordinate information flow and document production.
- The bank that demonstrates the best understanding and articulation of the credit should lead the investor presentation.
- The bank that can demonstrate recent and repeat experience in marketing Sterling bonds should lead the roadshow logistics.
- A bank should be allocated the task of leading the bookbuilding process, this bank should have the appropriate systems and experience.
- The league table above indicates the prominent bookrunning banks in the Sterling public bond market from January 2012 to date (February 2013).

Leading Bookrunners

The following tables highlight the bookrunners on some of the most recent Sterling and Sovereign bond issuance as at 14 February 2013.

FIGURE 77 – EXAMPLES OF INSTITUTIONS AND SOVEREIGNS ISSUING STERLING BONDS

Date	Issuer	Amount (£m)	Bookrunner
Feb-13	Network Rail	600	DB, RBC
Feb-13	Nordea Bank	400	HSBC, UBS
Feb-13	High Speed Rail	760	BNP, LBG, NAB, RBS, Scotia
Jan-13	European Investment Bank	500	BAR, DB, HSBC, JPM, RBC
Jan-13	Network Rail	750	DB, HSBC, RBS
Jan-13	Severn Trent Utilities	500	BNP, HSBC, RBS, SANT
Dec-12	Notting Hill Housing Trust	250	Barcap, GS, LBG
Dec-12	GlaxoSmithKline	1,400	DB, GS, HSBC, RBS
Dec-12	WM Treasury	200	BAR, RBS
Nov-12	Nestle	400	SANT, BAR, BNP, Citi, CS, DB, GS, HSBC, JPM, BASML, MIS, RBS, SG, UBS
Nov-12	Intercontinental Hotels	400	HSBC, LBG, RBS
Nov-12	APT Pipelines	350	BNP, RBS
Nov-12	Transport for London	300	BAR, HSBC, MS
Nov-12	Nordic Investment Bank	250	HSBC, RBC
Nov-12	Pohjola Bank	250	LBG
Nov-12	Swed Bank	250	NOM, RBS
Nov-12	London Stock Exchange	300	BAR, LBG, RBS
Oct-12	Export Development Canada	300	HSBC, RBC

Date	Issuer	Amount (US$m)	Bookrunner
Feb-13	Hungary	3,250	BNP, Citi, DB, GS
Feb-13	Ukraine	1,000	JPM, VTB Capital
Jan-13	United Kingdom	6,303	HSBC, JPM, MS, RBC
Jan-13	Lithuania	538	Barcap, Citi
Jan-13	Israel	2,000	BAR, Citi, GS
Jan-13	Sweden	5,386	Danske, GS, JPM, RBS
Jan-13	Republic of Portugal	3,329	Barcap, Banco Espirito, DB, MS
Jan-13	Colombia	1,000	DB, GS
Jan-13	Kingdom of Spain	9,328	Barcap, BBVA, Citi, GS, SANT, SG
Jan-13	Republic of Italy	7,979	Banca IMI, Barcap, CA, GS, JPM
Jan-13	Slovak Republic	1,959	HSBC
Jan-13	Kingdom of Belgium	5,223	Barcap, Citi, RBS, SG
Jan-13	Poland	1,308	BNP, DB, HSBC, UniCredit
Jan-13	Ireland	3,270	Barcap, Danske, Davy, RBS, SG
Jan-13	Republic of Turkey	1,500	BNP, DB, GS
Jan-13	Mexico	1,500	BAR, JPM
Dec-12	Republic of Lativa	1,250	BAR, DB, JPM,
Dec-12	Kingdom of Morocco	1,500	BAR, BNP, Citi, NAT
Dec-12	Republic of Turkey	1,000	BASML, HSBC, RBS
Nov-12	Mongolia	1,500	BASML, DB, HSBC, JPM, T&D Bank of Mongolia

Key

Bank of America Merrill Lynch	BASML	ING Groep	ING
Banco Santander	SANT	JP Morgan	JPM
Barclays Bank	BAR	Lloyds Banking Group	LBG
Barclays Capital	Barcap	Mitsubishi	MIS
BNP Paribas	BNP	Morgan Stanley	MS
Commerzbank AG	CZB	Natixis	NAT
Crédit Agricole	CA	National Australia Bank	NAB
Credit Suisse	CS	RBC Capital Markets	RBC
Deutsche Bank	DB	RBS	RBS
Goldman Sachs	GS	Société Générale	SG
HSBC	HSBC	UBS	UBS

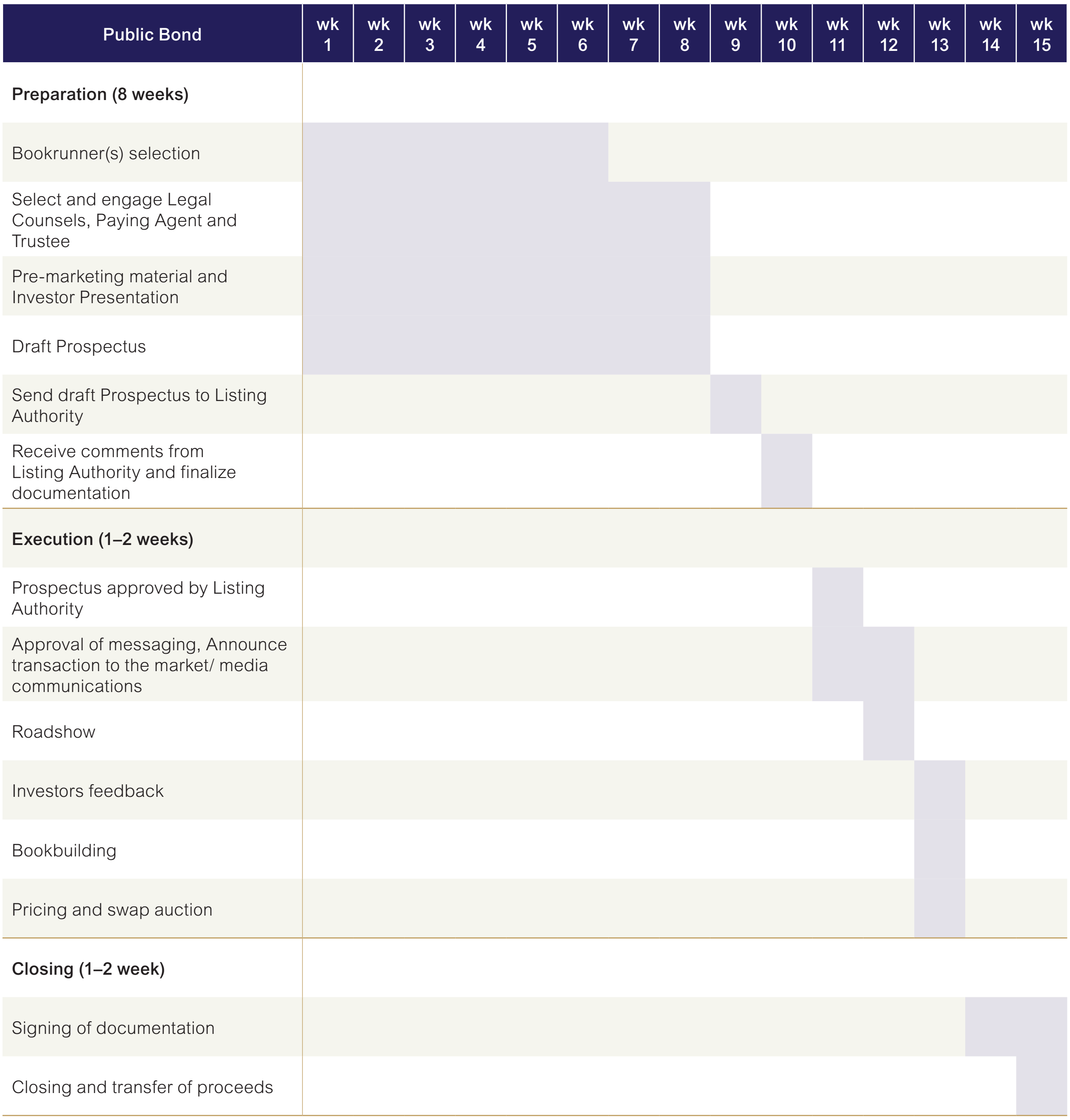
Source: Bloomberg, ThomsonOne

Timeline for Execution

Execution of a Sterling public bond can be achieved in as little as 12 weeks, once the credit rating has been assigned.

The Chart below sets out the typical profile of a bond issuance.

FIGURE 78 – A TYPICAL TIMETABLE FOR BOND ISSUANCE



Prospectus Preparation

The Prospectus is the main marketing document for the bond. The Prospectus will need to educate potential investors in great detail about the commercial and financial position of the States of Jersey.

- The Prospectus is a key document as it gives the issuer the opportunity to explain why the instrument is an attractive investment.

- A Preliminary Prospectus will have all the information about the issuer and the bonds being offered, except for the pricing information. The Final Prospectus will include the pricing information and will be delivered to investors along with a trade confirmation by the underwriter to confirm sales of the bonds.

- The required contents of the Prospectus are described below.

FIGURE 79 – OUTLINE OF A BOND PROSPECTUS FOR JERSEY

Business description	Other information
• A brief overview and history of the States of Jersey	• Overview of the bonds
• Description of the States of Jersey's structure, and operating activities	• Financial statements and auditor's report (last two years)
• Description of the economic profile of the States of Jersey	• Use of funds
• Detailed understanding of the relationship with the UK and Bank of England	• Terms and conditions of the bonds
• A section on risk factors related to the States of Jersey, the home country political and economic environment and the issuance of bonds along with mitigants to provide comfort over these risks	• Details of lead banks
• A section on the regulatory environment and any material litigation	• Details of anticipated rating of the notes
• A description of senior management / ministers	• Taxation considerations
• A description of governance processes	

Roadshow

The prospectus is the main marketing document. Following the completion of the prospectus, it would be necessary to market the bond through a roadshow, focusing on UK investors.

- A roadshow of UK investors can typically be conducted in 2-3 days and focuses on investors based in London and Scotland. A leg of the roadshow could be conducted in Jersey with specifically identified and invited investors. Investor meetings will provide the States of Jersey with an opportunity to present its credit proposition, the specifics of the deal, and respond to any questions that investors have.

- Investors will appreciate the opportunity to meet the States of Jersey's representatives, understand first hand the credit proposition and offering and ask questions.

- In addition to a series of one-on-one meetings, a global Investor call is recommended by Ernst & Young, allowing any non-UK investors to hear the prepared presentation of the bond from the States of Jersey first hand, with the opportunity to ask questions.

- Summarised below a number of the top investors in the Sterling bond market. The vast majority of these investors also have a track record of investing in 10 year sovereign public bonds.

FIGURE 80 – THE TOP INVESTORS IN THE STERLING BOND MARKET

A roadshow meeting will generally focus on a presentation of 30 minutes or so followed by questions.

The States of Jersey would likely conduct five or six bilateral meetings each day of the roadshow presenting the credit proposition and answering due diligence questions from potential investors in a 30-60 minute meeting, plus a group presentation and conference call with investors that are not able to meet the States of Jersey.

The bookrunner(s) will arrange and coordinate the logistics and participants of the roadshow. The bonds could be offered to local investors by timetabling an additional half day into the roadshow and could use local stockbrokers in combination with the bookrunning banks, however this would be at the discretion of the banks who will lead the sales and marketing of the bonds.

FIGURE 81 – STERLING ROADSHOW TIMETABLE

Day 1	London	One-on one meetings Group presentation
Day 2		One-on-one meetings Global investor Call
Day 3	Glasgow / Edinburgh	One-on-one meetings
Day 4	Jersey	Optional local one-on-one meeting

Bookbuilding

Bookbuilding is a short exercise, but is critical to the success of the issuance

Bookbuilding is the collection of bids for a certain quantum at a specified price. It is confidential to the bookrunner(s) and the States of Jersey.

The bookrunner(s) will advise the States of Jersey through a constant flow of market commentary, including advice on timing the bookbuilding so as to avoid conflict with a competing deal that may detract from the States of Jersey's issuance. Advice will also involve continued guidance and communication with potential investors of indicative pricing levels.

Once the book has been closed and all bids have been collected, the bookrunner(s) and States of Jersey can evaluate the demand levels and offers received and decide upon a profile of investor base and price level.

Bookbuilding will be best facilitated by bookrunner(s) that have the best relationship with the universe of Sterling investors, and will be able to leverage relationships to reduce the new issuance premium and drive the price down. We anticipate that the States of Jersey's bond will be extremely sought after and that the order book will be oversubscribed against the target issue amount.

- An oversubscribed book usually provides two possibilities:
- The issuance size is upscaled to take advantage of current offers

Competitive tension amongst investors drives improved terms for the issuer.

As the States of Jersey does not intend, and is in fact unable due to the borrowing cap, to increase its issuance size, we anticipate that it will be able to be selective about from which investors to accept offers and the terms of the final bond.

The States of Jersey may wish to allocate a small quantum of bonds to a diverse range of investors, or it may prefer its bond to be held by a small group of the largest institutional investors. All investors that receive allocations in the bond must have bid at or below the clearing price, which will have been guided by the bookrunners and the States of Jersey. If the States of Jersey wishes a specific investors to partake in the bond (for example, allowing for investment on-island), the bookrunner will manage the communication with that investor to ensure that its bid is below the anticipated clearing price.

The bookrunners, will keep the States of Jersey fully appraised of latest market data and pricing points, allowing live information to inform final terms.

At the end of the bookbuilding process, the bookrunner(s) and the States of Jersey will work out an allocation schedule, with all bidders below the clearing price eligible for an allocation of the bonds.

20. Appendix E – Ongoing Debt management Strategy Post Funding

Financial Reporting and Governance

Ongoing reporting requirements for a public Sterling bond are not onerous

There are a number of stakeholders who will seek to monitor the credit profile of the States of Jersey including ratings agencies and bond holders.

There is no ongoing requirement to meet or engage with bondholders.

- Bondholders may contact and request to meet the States of Jersey on an ad hoc basis. It would be good practice to engage with major bondholders, especially if a future issuance is being considered.

- Should the States of Jersey chose to meet with investors, it can arrange to meet with them directly.

Following the issuance of a public bond, the States of Jersey would be required to comply with the rules and regulations of the exchange(s) on which the bond is listed.

Ratings agencies would meet with the States of Jersey on an annual basis.

Assuming typical high investment grade Sterling bond terms, no financial covenants would exist. Therefore there would be no obligation to calculate financial covenants and report compliance with these.

The States of Jersey would be required to release annual accounts to the market and these must be published within six months of the end of the period to which they relate. It would be the States of Jersey's responsibility to ensure that the annual accounts and all other information that needs to be submitted to the exchange and ratings agencies are submitted in a timely manner.

Governance processes therefore need to be in place to ensure that accounts are filed on time and interaction with stakeholders occurs when necessary.

Covenant Considerations

Sterling public bonds include a number of common covenants however financial covenants for high investment grade issuers (i.e. Issuers within the AAA and AA rating bands) are not common

Sterling bond documentation typically includes a number of standard clauses to protect investors against a material deterioration in the credit quality of the issuer and to protect the position of investors in the capital structure.

As the States of Jersey does not have an existing bank facility or has not had any external debt in the recent past, there is no precedent for a suite of covenants that it has offered to previous lenders.

There is a fine balance between offering suitable covenants to gain sufficient interest in the deal and reducing flexibility for the issuer. The level of comfort investors gain from the covenants offered will be reflected in the pricing achieved.

Ernst & Young would not expect investors to require financial covenants.

Common non financial covenants in Sterling bond documentation include negative pledge, pari passu and cross default clauses.

- Negative pledge clause – stops the issuer pledging specific security to another party. Should the States of Jersey raise any additional debt subsequent to the proposed issuance, this covenant would prohibit it from assigning the new debt providers with specific security.

- Pari passu – ensures that the debt does and will rank alongside any other senior debt in terms of priority rankings. As the States of Jersey currently does not have any debt, this covenant would not be relevant to bond holders. However, should the States of Jersey raise additional debt subsequent to the potential bond issuance, this covenant would not allow the new debt providers to rank senior to the bond holders. The covenant protects the investor's security position.

- Cross default clause – if the issuer has more than one external debt agreement, a cross default clause says that if, for any reason, a default is recorded under one of the agreements, the other debt agreement(s) shall also register as being in default.

All of the covenants have minimal impact on the States of Jersey's profile as of today, but provide investors with comfort that they will retain at least equal rights to any lenders / investors in future external debt agreements.

Covenants are typically set according to precedents e.g. Isle of Man, and more recently, Cambridge University. Negative pledge, pari passu and cross default clauses were included in the Cambridge bond, we would not expect any further covenants for the States of Jersey.

Maintaining a Credit Rating

A credit rating is an ongoing obligation that the States of Jersey must maintain whilst public bonds are outstanding

Credit rating agencies are important stakeholders. Continued communication and provision of information is key to ensure that they are fully informed with developments.

Assigned credit ratings will be reviewed by the agencies on an ongoing basis. Any material changes in the credit quality of the issuer will be reflect in the assigned rating, therefore ratings upgrades and downgrades are a common occurrence.

The ratings agencies tend to take the approach of rating 'through the cycle', meaning that they aim to ensure that the rating reflects medium and long term trends rather than short term fluctuations.

Credit market investors, particularly bond investors, place a high level of reliance on the views of the ratings agencies therefore any ratings changes are likely to be reflected in the actions of investors trading the bonds in the secondary market.

- For instance, a downgrade of a rating will likely translate into the price of a bond falling in the secondary market and its yield correspondingly rising. Whilst this does not affect the interest paid by the issue (by virtue of the bond coupon being fixed), it would directly impact the cost of any subsequent issuance as investors will view the risk profile differently and expect to be rewarded accordingly.

Due to a vast number of high profile downgrades since the onset of the financial crisis, the media and general public are much more aware of the significance of credit ratings and therefore ratings changes are a larger driver of public perceptions than was historically the case.

The States of Jersey will be obliged to inform the agencies of any material developments and issues that arise and are potentially likely to affect its credit profile/quality. The States of Jersey are not obliged to provide investors of a public bond with this information. The agencies would provide guidance on the types of issues they would require the States of Jersey to report and provide information on. The agencies would also provide guidance on the rating rules and guidelines that the States of Jersey would be required to follow.

As part of the initial credit rating process, a lead analyst would be appointed to review and assess the States of Jersey credit profile. The lead analyst would be the key contact on the States of Jersey's credit rating within the agency.

Each year there will are a number of activities that need to be undertaken, these include:

- Present to each agency separately. The presentation should cover an update of the information provided in the initial rating submission. Any non-financial topics that have not been subject to change do not need to be covered in detail, however an update on financial information will be required each year.

- Payment of an annual fee (typically the same as the initial assessment fee).

21. Appendix F

Note on Limitations to Borrowing

Jersey Law limits the level of external debt that the States of Jersey can raise.

Paragraph 3 of Article 21 of the 'Public Finances (Jersey) Law 2005', Borrowing by the States of Jersey, states that "The States shall not authorize any borrowing if it would permit the total amount borrowed by the States at that time to exceed an amount equal to the estimated income of the States derived from taxation during the previous financial year." Paragraph 4 of Article 21 goes on to state that "in calculating the total amount borrowed by the States for the purpose of paragraph (3) there shall not be taken into account –

(a) any amount borrowed from a third party by a company owned or controlled by the States; and

(b) the liability of a company owned or controlled by the States under any guarantee or indemnity given by the company."

Regulation 9 (7) of Chapter 3 of the Public Finances (Transitional Provisions) (No.2) Regulations 2005, states that "for the purpose of this Regulation,

- borrowing by the States shall be taken to include the giving of a guarantee in the name of the States and the provision of an indemnity in the name of the States; and

- the liability of the States in respect of any such guarantee or indemnity shall be taken as an amount borrowed by the States."

Based on The Public Finances (Jersey) Law 2005 and The Public Finances (Transitional Provisions) (No.2) Regulations 2005, the annual borrowing cap of the States of Jersey is dictated by the revenue generated through taxation in the previous year less current borrowings of the States of Jersey as highlighted in the table.

It is assumed in this report that the cap on external debt is calculated based upon 2012 as this is the most recent cap based on outturn full year financial results.

FIGURE 82 – CALCULATION OF THE MAXIMUM BORROWING REQUIREMENTS FOR THE STATES OF JERSEY UNDER THE PUBLIC FINANCE LAW

£m	2011[1]	2012[2]	2013[2]	2014[2]	2015[2]	2016
Income tax	409.3	430.0	450.0	470.0	500.0	-
Budget measure	-	-	7.6	7.6	7.6	-
Goods and Service Tax	66.3	77.7	79.8	82.0	84.5	-
Imports Duty	51.1	51.1	52.9	53.0	53.1	-
Stamp Duty	22.6	22.9	24.5	27.7	29.0	-
Total taxes	549.3	581.7	614.8	640.3	674.2	-
Less Guarantees[3]	20.8	20.8	20.8	20.8	20.8	
Net amount	528.5	560.9	594.0	619.5	653.4	-
Annual borrowing cap	-	528.5	560.9	594.0	619.5	653.4

Sources: States of Jersey Financial Report and Accounts 2011; Medium Term Financial Plan.

(1) These numbers are based on 2011 Actual tax receipts, page 16 of the Financial Report and Accounts for 2011.

(2) These numbers are based on 2012-2015 forecast tax receipts as reported in the draft Medium Term Financial Plan (MTFP) (Project P.69/2012) – page 18.

(3) Note: These guarantees are not recognised on the States of Jersey's balance sheet but are required to be included in the calculation. As at 31.12.11 they were made up of £14.9m to JNWWC, £3.8m Jersey Arts Trust, £1.7m for Student Loan Guarantees and £0.4m for Small Firms Loan Guarantee Scheme. It is expected that they will continue at these levels or decrease slightly.

22. Appendix G – Borrowing through a Public Rated Bond: Credit Ratings

Credit Rated Peers

If the States are to issue a public rated bond, then the States needs to take a credit rating.

The broad peer group for the States of Jersey consists of smaller, relatively wealthy sovereign states, with a high proportion of national income derived from the financial services sector, such as Lichtenstein, Bermuda, Singapore and Hong Kong. Treasury has taken Jersey's peers as being of a rating profile of AA- or better.

Jersey compares favourably to its peers with regard in Government debt based metrics, as the States currently has no external debt. However, using GVA as a proxy for GDP, the States GDP metrics compare less well, as, per the GVA report for 2011, Jersey real GVA reduced in the year.

FIGURE 83 – CREDIT RATED PEERS: A COMPARISON WITH JERSEY

	Guernsey*	Isle of Man	Bermuda	Hong Kong	Liechtenstein	Singapore	Jersey
Moody's	Not Rated	Aaa	Aa2	Aa1	Aaa	Aaa	-
Standard & Poor's	AA+	AA+	AA-	AAA	AAA	AAA	-
Fitch	Not Rated	Not Rated	AA	AAA	Not Rated	AAA	-
GDP per capita (US$)	49,610	70,151	89,314	34,457	141,301	50,127	59,385
Real GDP (% change, annual)	0.7%	2.1%	NA	5.0%	2.3%	4.9%	(0.8)%
Real GDP per capita (% change, annual)	0.4%	2.1%	(3.1)%	4.3%	1.7%	2.7%	(1.7)%
General government balance (% of GDP)	(1.0)%	(1.4)%	NA	4.0%	(1.5)%	8.1%	0.0%
General government debt (% of GDP)	0.0%	13.4%	2.6%	0.6%	0.0%	108.3%	0.0%
Net general government debt (% of GDP)	(105.4)%	(50.0)%	(9.8)%	(34.7)%	(96.7)%	(91.6)%	(1.8)%
General government interest exp. (% of revenues)	0.0%	2.0%	6.9%	0.1%	0.0%	0.0%	0.0%
Consumer price index (average; % change, annual)	3.1%	6.2%	2.6%	5.3%	1.0%	5.3%	4.5%

*NB Guernsey withdrew its rating at the end of January 2013

Potential Downsides of Obtaining a Credit Rating

There are considerations in obtaining a credit rating, such as the impact, financial and political, of potential changes to the ratings

Obtaining a public rating has clear reputational risks, in that a downgrade can occur for reasons completely exogenous to the States of Jersey (for example, a change in rating methodology applied by an agency).

Many stakeholders, and the general public, may not have the time or knowledge to understand the nuances of any adverse changes to a credit rating, even where it is not the 'fault' of the issuer.

Possessing and maintaining a strong relationship with rating agencies is an important part of mitigating downside risks.

The close link to the UK means that factors beyond the States of Jersey's control may affect its ratings profile.

The States of Jersey would be rated on a standalone basis, but the relationship with the UK being Jersey's single largest trading partner, with a shared currency and that Jersey is a British Crown Dependency – indicates that the perception of Jersey's credit profile will likely be affected by the position of the UK.

Whilst Jersey's rating should not be capped by the UK rating under any agency, a UK rating downgrade would create negative rating pressure on the States of Jersey's rating.

- Moody's was the first rating agency to downgrade the outlook of the UK to negative, doing so in February 2012. When Moody's downgraded the outlook of the UK to negative, it also declared that it will be re-examining the UK's rating in the first few months of 2013. On Friday, 22 February 2013, Moody's downgraded the UK's credit rating from Aaa to Aa1 with a stable outlook.

- S&P maintains the UK at a rating of AAA with a stable outlook. This rating and outlook was most recently reaffirmed in July 2012. Outlooks are designed to reflect a 3 to 5 year time horizon for rating action. Whilst we believe S&P is very unlikely to assign Jersey an 'AAA' rating, Ernst & Young advise that a prospective AA+ Jersey rating is most stable under S&P.

- Fitch, like Moody's, rate the UK at AAA with a negative outlook. The probability of an imminent Fitch downgrade of the UK is lower than that for Moody's. Fitch state the probability is 50/50 of a downgrade sometime over the next two years. The UK sovereign outlook for Fitch is therefore less likely to disrupt the Jersey rating profile than Moody's, but more so than S&P.

Maintaining two credit ratings is beneficial for two reasons. First, where the ratings are equivalent it strengthens investor confidence in the stability of the rating. Second, in the event only one of the ratings is downgraded, it can limit the impact on the price of outstanding bonds, and it eases the challenge of communication to non-financial stakeholders. There is, however, a cost associated with two ratings, namely the annual monitoring fee, as well as the additional time spent dealing with a second analytical team.

Overview of Credit Ratings

Ernst & Young's assessment of ratings agencies suggests that obtaining ratings assessments from S&P and Fitch would be an appropriate strategy

The table below summarises Ernst & Young's assessment of the ratings agencies.

FIGURE 84 – ERNST & YOUNG'S ASSESSMENT OF RATING AGENCIES

Factor	Comment
Number of ratings	There is precedent for sovereign issuers accessing the market with one rating, however two is more common.
Experience of agency teams	S&P and Fitch appeared to be offering a team that would provide a greater level of senior involvement.
Timing	Fitch committed to the shortest turnaround time (4-6 weeks), however S&P and Moody's only differed by a couple of weeks (6-8 week and 7-8 weeks indicated respectively).
Cost	Whilst Moody's proposed the lowest price, this was viewed in light of the potential ratings outcome.
Information requirements	Fitch and S&P appeared to be the most willing to work flexibly with the data available.
Ratings outcome	Whilst we would currently expect all agencies to arrive at the same outcome (AA+ equivalent), we would have expected the Moody's rating to be the least stable due to lack of clarity in the rating methodologies and potential imminent downgrade of the Isle of Man, a close peer of the States of Jersey.

Overview Of Risks And Mitigations For Public Rated Bond Issuance

Ernst & Young advise that there are a number risks relating to the finance raising that need to be identified and to the extent possible, mitigated

FIGURE 85 – OVERVIEW OF RISKS AND MITIGATIONS FOR BOND ISSUANCE

Risk	Description	Potential mitigation
Execution risk	• Due to the fact that capital markets transactions are priced with respect to market rates. There is the risk that an adverse outcome occurs if the deal is priced at the wrong point in time when the market is unreceptive and sufficient demand does not exist.	• Appointment of bookrunner who can demonstrate deep expertise in the Sterling public bond market. Suitable bookrunners will also be able to clearly articulate specific strategies they intend to deploy in order to achieve the best value pricing.
Subscription risk	• The risk that not enough investors subscribe to the debt offering – in an underwritten deal this risk is mitigated to an extent however would still likely result in adverse view of the securities.	• Appointment of bookrunner who can demonstrate a well defined marketing and sales plan, have depth of resource in sales, and who can demonstrate an insight into likely investors and their specific preferences and requirements.
Stakeholder risk	• The ultimate stakeholders are the residents of the island who are represented by the States of Jersey.	• A comprehensive approval process that ensures due process is followed.
Media risk	• The link to the political landscape ensures that sovereign issuances are subject to a high level of media scrutiny and therefore any success or failure may be amplified through press reports.	• Media communications strategy to be developed, actions and decisions documented to ensure potential future media criticism can be coherently and robustly addressed.
Rating downgrade risk	• Obtain a public credit rating and subsequently experience a downgrade.	• Maintaining a strong relationship and clear dialogue with the ratings agencies such that the States of Jersey can present the context of any potential issues or queries of the agencies.
Cash flow variance	• Risk that the States of Jersey is unable to make interest payments or contributions to any bond repayment fund that is set up or risk that Project costs are more than funds raised.	• Prudent to be applied when concluding on the level of debt that the State of Jersey can afford to service. Modelling of stressed scenarios, contingency plans to enact in the event that debt servicing becomes more challenging. Ensure debt raised when certainty over Project costs.
Regulatory and legal risk	• The risk that the debt raising and marketing, and ongoing obligations relating to the issuance do not abide by relevant laws, regulations and legal documents. For example, the issuance proceeds must be such that they do not cause the States of Jersey to breach the borrowing cap set out in the Public Finances (Jersey) Law 2005.	• Appointment of legal advisors who can demonstrate knowledge of the State of Jersey's legal regime and are able to prove expertise in public capital markets debt matters and have experience of recent relevant public bond transactions.

PART G – SUMMARY TABLES

23. Summary Table A – States Income 2014

	Outturn	MTFP (July 2012)		Budget 2013 (Dec 2012)		Budget 2014 (Oct 2013)
	2012	2013	2014	2013	2014	2014
	£'000	£'000	£'000	£'000	£'000	£'000
Income Tax						
Personal Income Tax	351,121	377,000	394,000	377,000	394,000	394,000
Companies	79,339	77,000	80,000	79,965	82,965	82,965
Provision for Bad Debt		(4,000)	(4,000)	(2,000)	(2,000)	(2,000)
	430,460	450,000	470,000	454,965	474,965	474,965
Original Budget Measures		7,600	7,600			
Goods and Services Tax (GST)	79,559	79,761	81,955	79,761	81,955	81,955
Impôts Duties						
Impôts Duties Spirits	4,091	4,157	4,133	4,161	4,137	4,747
Impôts Duties Wine	6,783	7,248	7,504	7,256	7,512	7,729
Impôts Duties Cider	927	1,039	1,107	1,040	1,108	930
Impôts Duties Beer	5,047	5,732	5,758	5,738	5,764	5,559
Impôts Duties Tobacco	15,825	12,392	11,813	14,004	13,425	14,789
Impôts Duties Fuel	20,396	21,221	21,537	21,135	21,451	20,363
Impôts Duties Goods (Customs)	328	150	150	150	150	150
Vehicle Emissions Duty (VED)	839	1,000	1,000	1,050	1,050	924
	54,236	52,939	53,002	54,534	54,597	55,191
Stamp Duty						
Stamp Duty	15,404	20,478	23,427	20,478	23,427	23,127
Probate	4,069	2,500	2,500	2,500	2,500	2,500
Stamp Duty on Share Transfer (LTT)	1,699	1,551	1,775	1,551	1,775	1,775
	21,172	24,529	27,702	24,529	27,702	27,402
Total Taxation Revenue	**585,427**	**614,829**	**640,259**	**613,789**	**639,219**	**639,513**
Other States Income						
Net Investment Income	4,166	3,721	3,679	3,721	3,679	3,679
Dividends and Returns	18,442	8,319	11,186	8,319	11,186	11,186
Jersey Financial Services Commission Fees	3,685	3,700	3,700	3,700	3,700	3,700
Returns from States Trading Operations	1,671	1,691	1,731	1,691	1,731	1,731
EUSD Retention Tax	1,464	1,500	-	1,500	-	-
Income Tax Penalties	1,035	1,071	1,071	1,071	1,071	1,071
Fines and Other Income	463	543	559	543	559	559
	30,926	20,545	21,926	20,545	21,926	21,926
Island Rate Income from Parishes	11,380	11,670	12,032	11,670	12,032	12,032
Total States Income	**627,733**	**647,044**	**674,217**	**646,004**	**673,177**	**673,471**

1. The States decision not to approve the increases in Impôts duty on fuel was partly offset by additional increases on tobacco resulting in a reduction of £1.04 million in the MTFP States income targets following the 2013 Budget

2. The impact of the 2014 Budget proposals amounts to £294,000 in 2014 with the Income Tax proposals in respect of year of assessment 2014 not affecting the States accounts until 2015.

24. Summary Table B – Proposed Allocation of Growth Expenditure for 2014 and 2015

States Funded Bodies	2014 Gross Expenditure Allocation £'000	2014 Income Allocation £'000	2014 Net Expenditure Allocation £'000	2015 Gross Expenditure Allocation £'000	2015 Income Allocation £'000	2015 Net Expenditure Allocation £'000
Ministerial Departments						
Chief Minister	410		410	410		410
- Grant to the Overseas Aid Commission			–			–
Economic Development			–			–
Education, Sport and Culture			–			–
Department of the Environment			–			–
Health and Social Services			–			–
Home Affairs	50		50	50		50
Housing			–			–
Social Security	750		750	1,000		1,000
Transport and Technical Services	1,000		1,000			–
Treasury and Resources			–			–
Non Ministerial States Funded Bodies						
- Bailiff's Chambers			–			–
- Law Officers' Department			–			–
- Judicial Greffe			–			–
- Viscount's Department			–			–
- Official Analyst			–			–
- Office of the Lieutenant Governor			–			–
- Office of the Dean of Jersey			–			–
- Data Protection Commission			–			–
- Probation Department			–			–
- Comptroller and Auditor General			–			–
States Assembly and its services			–			–
Allocation of Growth Expenditure	**2,210**	**0.0**	**2,210**	**1,460**	**0.0**	**1,460**

25. Summary Table C – Proposed Capital Programme for 2014 – Funding Sources

	£'000 2014	£'000 2014
Departmental Capital Programme	**66,692**	
Funding Sources		
Consolidated Fund		(2,049)
Strategic Reserve *		(10,200)
Contribution from Currency Fund		(3,000)
JPH receipts		(4,480)
Additional Funding from Consolidated Fund – Housing Repayment		(26,472)
Repayment of Le Squez and Pomme D'Or Farm		(11,250)
Use of Jersey Post Dividend		(698)
Repayment of JT Preference Shares		(4,743)
Use of Carry Forwards 2013 to 2014		(3,300)
Funded from the Central Planning Vote		(500)
Funding Available		**(66,692)**
Social Housing Programme	22,200	
Housing Funding Sources		(22,200)
TOTAL CAPITAL EXPENDITURE (INCOME)	**88,892**	**(88,892)**
Funding from Consolidated Fund (Main allocation)		**2,049**
Funding from Other Sources (Income to Consolidated Fund etc)		**64,643**
Housing Funding		**22,200**
TOTAL FUNDING		**88,892**

* subject to the approval by the States of the use of the Strategic Reserve Fund to fund the future redevelopment of hospital services within the Island from 2014.

26. Summary Table D – Proposed Capital Programme for 2014

	£'000 2014 Budget
Chief Minister's	
Web Development	170
JDE Development & Upgrade	370
Application remediation Windows 8	500
Chief Minister's total	**1,040**
Education, Sport and Culture	
School ICT	1,000
Autism Support Unit	1,066
FB Fields Running Track	810
Les Quennevais Artificial Pitch	650
St James Centre	2,500
Additional Primary School Accommodation (Phase 1)	8,188
Sports Strategy Infrastructure (Phase 1)	1,550
Education, Sport and Culture total	**15,764**
Department of the Environment	
Fisheries Vessels	100
Met Radar Refurbishment/ Upgrade	350
Countryside Infrastructure	200
Department of the Environment total	**650**
Health & Social Services	
Future Hospital (Phase 1)	10,200
Main Theatres Project	1,837
Future Hospital - Planning	500
Integrated Assesment and Intermediate Care	500
Refurbishment of Sandybrook	1,700
Health & Social Services total	**14,737**
Home Affairs	
Police Station Relocation - Tranche 4	1,000
Home Affairs total	**1,000**
Transport and Technical Services	
Infrastructure Rolling Vote	6,657
Refurbishment of Clinical Waste Incinerator	300

	£'000 2014 Budget
Liquid Waste Strategy (Phase 1)	10,100
Ash Cells & La Collette Headland	1,051
New Public Recycling Centre	2,050
Bottom Ash Recycling	1,538
Scrap Yard Capital Basic Infrastructure	1,025
EFW Plant La Collette Replacement Assets	1,586
Project - Green Street Car Park	1,500
Transport and Technical Services total	**25,807**
Treasury & Resources (inc. JPH)	
Tax Transformation Programme & IT systems	500
Demolition of Fort Regent Pool	750
Fiscal Stimulus and Parish Projects	1,252
Treasury & Resources (inc. JPH) total	**2,502**
Vehicle replacement (additional from consolidated fund)	**1,500**
Replacement assets	**3,692**
Total Projects - Capital Allocation	**66,692**
Housing	
Social Housing Programme	22,200
Total Programme	**88,892**

27. Summary Table E – Proposed Capital Allocation to States Trading Operations for 2014

	£ 2014 Budget
Minor Capital Assets	331,000
Jersey Airport	**331,000**
Minor Capital Assets	368,000
Jersey Harbours	**368,000**
Car Park Maintenance and Refurbishment	561,000
Jersey Car Parking	**561,000**
Vehicle and Plant Replacement	1,091,000
Jersey Fleet Management	**1,091,000**

28. Summary Table F – Consolidated Fund Forecast for 2014

Actual	Consolidated Fund	MTFP		Budget 2013		Revised Forecast for 2014 Budget	
2012		2013	2014	2013	2014	2013	2014
£'000		£'000	£'000	£'000	£'000	£'000	£'000
47,176	**Opening Balance**	**32,738**	**19,717**	**32,738**	**18,677**	**31,160**	**12,099**
(27,100)	Proposed Capital Expenditure Allocation - Housing Schemes						
	Other Fund Adjustments - Return of Housing Capital		27,000		27,000		27,000
	Other Fund Adjustments - Allocation to Capital Programme		(26,472)		(26,472)		(26,472)
20,000	Repayment of JT Preference Dividends		(4,743)		(4,743)		(4,743)
	Other Fund Adjustments - Allocation to Capital Programme	(8,500)		(8,500)		(8,500)	
	Other Fund Adjustments - Allocation to Innovation Fund					(5,000)	
7,000	Other Fund Adjustment - Earmarked Carry Forward from 2012 to Fund Capital	(7,000)		(7,000)		(7,000)	
	Other Fund Adjustment - Earmarked Carry Forward from 2013 to Fund Capital	3,300	(3,300)	3,300	(3,300)	3,300	(3,300)
	Other Fund Adjustment - Jersey Post Special Dividend 2012 to Fund Capital	(1,528)	(698)	(1,528)	(698)	(1,528)	(698)
	Other Fund Adjustment - Apply Strategic Reserve contribution to Future Hospital project (Phase 1)						(10,200)
	Other Fund Adjustment - Apply Currency Fund contribution to Liquid Waste Strategy (Phase 1)						(3,000)
(27,088)	Other Fund Adjustments						
	Proposed transfer from Strategic Reserve						10,200
	Transfer from Currency Fund						3,000
11,172	**Forecast Surplus/(Deficit) for the year**	**707**	**59**	**(333)**	**(981)**	**(333)**	**(981)**
	Budget measures 2014 Budget						294
	Proposed variations to the Capital Programme 2014 requiring a reduced contribution from the Consolidated Fund in 2014						2,510
	Estimated Consolidated Fund Balance						
31,160	**Central scenario**	**19,717**	**11,563**	**18,677**	**9,483**	**12,099**	**5,709**

1. The States decision not to approve the increases in Impôts duty on fuel was partly offset by additional increases on tobacco resulting in a reduction of £1.04 million in the MTFP States income targets following the 2013 Budget.
2. Following the production of the 2012 Financial Accounts the balance on the Consolidated Fund at the beginning of 2013 had reduced slightly and is forecast to reduce to £12 million by the end of 2013. This is largely due to the allocation to the Innovation Fund being made in 2013 when originally forecast for 2012.
3. The impact of the 2014 Budget proposals amounts to £294,000 in 2014 with the Income Tax proposals in respect of year of assessment 2014 not affecting the States accounts until 2015.
4. The contribution from the Strategic Reserve of £10.2 million in 2014 is subject to the States approval of the use of the Strategic Reserve to fund the future redevelopment of hospital services within the Island from 2014.